United Nations A/CN.9/471/Add.6

General Assembly

Distr.: General
10 February 2000

Original: English

United Nations Commission on International Trade Law
Thirty-third session
New York, 12 June-7 July 2000

Privately financed infrastructure projects: draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

Chapter V. Duration, extension and termination of the project agreement

Contents

		Paragraphs	Page
Legislative recommendations			2
Notes on the legislative recommendations		1-62	4
A.	General remarks	1	4
B.	Duration of the project agreement	2-5	4
C.	Extension of the project agreement	6-8	5
D.	Termination	9-35	6
1.	Termination by the contracting authority	14-27	7
2.	Termination by the concessionaire	28-33	11
3.	Termination by either party	34-35	12
E.	Consequences of expiry or termination of the project agreement	36-62	12
1.	Transfer of project-related assets	37-42	13
2.	Financial arrangements upon termination	43-49	15
3.	Wind-up and transitional measures	50-62	18

V.00-50941 (E)

Legislative recommendations

For host countries wishing to promote privately financed infrastructure projects it is recommended that the following principles should be implemented by the law:

Duration and extension of the project agreement (see paras. 2-8)

Recommendation 60. The duration of the concession should be specified in the project agreement.

Recommendation 61. The term of the concession should not be extended, except in those circumstances specified in the law, such as:

(a) Completion delay or interruption of operation due to the occurrence of circumstances beyond either party's reasonable control;

(b) Project suspension brought about by acts of the contracting authority or other public authorities;

(c) To allow the concessionaire to recover additional costs arising from requirements of the contracting authority not originally foreseen in the project agreement that the concessionaire would not be able to recover during the normal term of the project agreement.

Termination of the project agreement (see paras. 9-35)

Termination by the contracting authority

Recommendation 62. The contracting authority should have the right to terminate the project agreement:

(a) In the event that it can no longer be reasonably expected that the concessionaire will be able or willing to perform its obligations, owing to insolvency, serious breach or otherwise;

(b) For reasons of public interest, subject to payment of compensation to the concessionaire.

Termination by the concessionaire

Recommendation 63. The concessionaire should have the right to terminate the project agreement under exceptional circumstances specified in the law, such as:

(a) In the event of serious breach by the contracting authority or other public authority as regards the fulfilment of their obligations under the project agreement;

(b) In the event that the concessionaire's performance is rendered substantially more onerous as a result of variation orders or other acts of the contracting authority, unforeseen changes in conditions or acts of other public authorities and that the parties have failed to agree on an appropriate revision of the project agreement.

Termination by either party

Recommendation 64. Either party should have the right to terminate the project agreement in the event that the performance of its obligations is rendered impossible by

the occurrence of circumstances beyond either party's reasonable control. The parties should also have the right to terminate the project agreement by mutual consent.

Consequences of expiry or termination of the project agreement (see paras. 36-62)

Transfer of assets to the contracting authority or to a new concessionaire

Recommendation 65. The project agreement should lay down the criteria for establishing, as appropriate, the compensation to which the concessionaire may be entitled in respect of assets transferred to the contracting authority or to a new concessionaire or purchased by the contracting authority upon expiry or termination of the project agreement.

Financial arrangements upon termination

Recommendation 66. The project agreement should stipulate how compensation due to either party in the event of termination of the project agreement is to be calculated, providing, where appropriate, for compensation for the fair value of works performed under the project agreement and for losses, including lost profits.

Wind-up and transfer measures

Recommendation 67. The project agreement should set out, as appropriate, the rights and obligations of the parties with respect to:

(a) The transfer of technology required for the operation of the facility;

(b) The training of the contracting authority's personnel or of a successor concessionaire in the operation and maintenance of the facility;

(c) The provision, by the concessionaire, of operation and maintenance services and the supply of spare parts, if required, for a reasonable period after the transfer of the facility to the contracting authority or to a successor concessionaire.

Notes on the legislative recommendations

A. General remarks

1. Most privately financed infrastructure projects are undertaken for a certain period, at the end of which the concessionaire transfers to the contracting authority the responsibility for the operation of the infrastructure facility. Section B deals with elements to be taken into account when establishing the concession period. Section C deals with the question of whether and under what circumstances the project agreement may be extended. Section D considers circumstances that may authorize the termination of the project agreement prior to the expiry of its term. Lastly, section E deals with the consequences of the expiry or termination of the project agreement, including the transfer of project assets and the compensation to which either party may be entitled upon termination, and the wind-up of the project.

B. Duration of the project agreement

2. The laws of some countries contain provisions that limit the duration of infrastructure concessions to a certain number of years. Some laws establish a general limit for most infrastructure projects and special limits for projects in particular infrastructure sectors. In some countries there are maximum duration periods only for certain infrastructure sectors.

3. The desirable duration of a project agreement may depend on a number of factors, such as the operational life of the facility; the period during which the service is likely to be required; the expected useful life of the assets associated with the project; how changeable the technology required for the project is; and the time needed for the concessionaire to repay its debts and amortize the initial investment. The notion of economic "amortization", in this context, refers to the gradual charging of the investment made against project revenue on the assumption that the facility would have no residual value at the end of the project term. Given the difficulty of establishing a single statutory limit for the duration of infrastructure projects, it is advisable to provide the contracting authority with some flexibility to negotiate, in each case, a term that is appropriate to the project in question.

4. In some legal systems, this result is achieved by provisions that require that all concessions should be subject to a maximum duration period, without specifying any number of years. Sometimes the law only indicates which elements are to be taken into account for determining the duration of the concession, which may include the nature and amount of investment required to be made by the concessionaire and the normal amortization period for the particular facilities and installations concerned. Some project- or sector-specific laws provide for a combined system requiring that the project agreement should provide for the expiry of the concession at the end of a certain period or once the debts of the concessionaire have been fully repaid and a certain revenue, production or usage level has been achieved, whichever is the earliest.

5. However, where it is found necessary to adopt statutory limits, the maximum period should be sufficiently long to allow the concessionaire to repay its debts fully and to achieve a reasonable profit. Furthermore, it may be useful to authorize the contracting authority, in exceptional cases, to agree to longer concession periods, taking into account the amount of the investment and the required recovering period, and subject to special approval procedures.

C. Extension of the project agreement

6. In the contracting practice of some countries, the contracting authority and the concessionaire may agree on one or more extensions of the concession period. More often, however, domestic laws only authorize an extension of the project agreement under exceptional circumstances. In this case, upon expiry of the project agreement the contracting authority is normally required to select a new concessionaire, normally using the same procedures applied to select the concessionaire whose concession has expired (for a discussion of selection procedures, see chap. III, "Selection of the concessionaire").

7. A number of countries have found it useful to require that exclusive concessions be rebid from time to time rather than freely extended by the parties. Periodic rebidding may give the concessionaire strong performance incentives. The period between the initial award and the first (and subsequent) rebidding should take into account the level of investment and other risks faced by the concessionaire. For example, for solid waste collection concessions not requiring heavy fixed investments, the periodicity may be relatively short (three to five years, for example), whereas longer periods may be desirable for power or water distribution concessions. In most countries, rebidding coincides with the end of the project term, but in others a concession may be granted for a long period (say 99 years), with periodic rebidding (for instance, every 10 or 15 years). In the latter mechanism, which has been adopted in a few countries, the first rebidding occurs before the concessionaire has fully recouped its investments. As an incentive to the incumbent operator, some laws provide that the concessionaire may be given preference over other bidders in the award of subsequent concessions for the same activity. However, the concessionaire may have rights to compensation if it does not win the next bidding round, in which case all or part of the bidding proceeds may revert to the incumbent concessionaire. Requiring that the winning bidder should pay off the incumbent concessionaire for any property rights and for the investment not yet recovered reduces the longer-term risk faced by investors and lenders and provides them a valuable exit option (see paras. 39 and 40).

8. Notwithstanding the above, it is advisable not to exclude entirely the option to negotiate an extension of the concession period under certain specified circumstances. The duration of an infrastructure project is one of the main factors taken into account in the negotiation of financial arrangements and has a direct impact on the price of the services provided by the concessionaire. The parties may find that an extension of the project agreement (as a substitute for or combined with other compensation mechanisms) may be a useful option to deal with unexpected impediments or other changes of circumstances arising during the life of the project. Such circumstances may include any of the following: extension to compensate for project suspension or loss of profit due to the occurrence of impeding events (see chap. IV, "Construction and operation of infrastructure", paras. 131-139); extension to compensate for project suspension brought about by the contracting authority or other public authorities (see chap. IV, "Construction and operation of infrastructure", paras. 140 and 141); or extension to allow the concessionaire to recover the cost of additional work required to be done on the facility and which the concessionaire would not be able to recover during the normal term of the project agreement without unreasonable tariff increases (see chap. IV, "Construction and operation of infrastructure", paras. 73-76). For purposes of transparency and accountability, in some countries the extension of the concession period is subject to a global cumulative limit or requires the approval of a specially designated public authority.

D. Termination

9. The grounds for termination of the project agreement before the expiry of its term and the consequences of any such termination are often dealt with in domestic legislation. Usually the law authorizes the parties to terminate the project agreement following the occurrence of certain types of events. The main interest of all parties involved in a privately financed infrastructure project is to ensure the satisfactory completion of the facility and the continuous and orderly provision of the relevant public service. Given the serious consequences of termination, as provision of the service may be interrupted or even discontinued, termination should under most circumstances be regarded as a measure of last resort. The conditions for the exercise of this right by either party should be carefully considered. While they may not need to be identical, it is generally desirable to achieve a broadly equitable balance of rights and conditions regarding termination for both parties.

10. In addition to identifying the circumstances or types of events that may give rise to a termination right, it is advisable for the parties to consider appropriate procedures to establish whether there are valid grounds for terminating the project agreement. Of particular importance is the question whether the project agreement may be unilaterally terminated or whether termination requires a decision by a judicial or other dispute settlement body.

11. The concessionaire is usually not allowed to terminate the project agreement without cause and in some legal systems termination by the concessionaire even in the event of breach by the contracting authority requires a final judicial decision. However, in some countries, pursuant to rules applicable to contracts with government entities, such a right may be exercised by public authorities, subject to payment of compensation to the concessionaire. In other countries, however, an exception is made in the case of public service concessions, whose contractual nature is found to be incompatible with unilateral termination rights. Lastly, some legal systems do not recognize unilateral termination rights for public authorities. However, project promoters and lenders would be concerned about the risk of premature or unjustified termination by the contracting authority, even where a decision to terminate might be subject to review through the dispute settlement mechanism. It should also be noted that giving the contracting authority the unilateral right to terminate the project agreement would not be an adequate substitute for well-designed contractual mechanisms of performance monitoring or for appropriate guarantees of performance (see chap. IV, "Construction and operation of infrastructure", paras. 80-97 and 108-120).

12. Provisions concerning termination should therefore be brought into line with the remedies for breach provided in the project agreement. In particular, it is useful to distinguish the conditions for termination from those for step-in by the contracting authority (see chap. IV, "Construction and operation of infrastructure", paras. 143-146). It is also important to consider the contracting authority's termination rights against the background of the financing agreements negotiated by the concessionaire with its lenders. In most cases, events that may lead to the termination of the project agreement would also constitute events of default under the loan agreements, with the consequence that the entire outstanding debt of the concessionaire may fall due immediately. It would thus be useful to attempt to avoid the risk of termination by allowing the lenders to propose another concessionaire when termination of the project agreement with the original concessionaire appears imminent (see chap. IV, "Construction and operation of infrastructure", paras. 108-120).

13. In the light of the above, it is generally advisable to provide that the termination of the project agreement in most cases require a final finding by the dispute settlement body provided in the agreement. Such a requirement would reduce concerns about premature or unjustified recourse to termination. At the same time, it would not preclude the taking of appropriate

measures to ensure the continuity of the service, pending the final decision of the dispute settlement body, as long as contractual remedies for breach, such as step-in rights for the contracting authority and the lenders, are provided in the project agreement. In countries where such a requirement would not be consistent with general principles of administrative law applicable to government contracts, it might be important to ensure, at least, that the contracting authority's right to terminate the project agreement should be without prejudice to the concessionaire's right to seek subsequent judicial review of the contracting authority's decision to terminate.

1. Termination by the contracting authority

14. The contracting authority's termination rights usually relate to three categories of circumstances: serious breach by the concessionaire; insolvency or bankruptcy of the concessionaire; and termination for reasons of public interest.

(a) Serious breach by the concessionaire

15. The contracting authority has the duty to ensure that public services are provided in accordance with applicable laws, regulations and contractual provisions. Thus, a number of domestic laws expressly recognize the contracting authority's right to terminate the project agreement in the event of breach by the concessionaire. Because of the disruptive effects of termination and in the interest of preserving the continuity of the service, it is not advisable to regard termination as a sanction for each and any instance of unsatisfactory performance by the concessionaire. On the contrary, it is generally advisable to resort to the extreme remedy of termination only in cases of "particularly serious" or "repeated" failures to perform, especially when it can no longer be reasonably expected that the concessionaire will be able or willing to perform under the project agreement. Many legal systems use specific technical expressions to refer to situations where the degree of breach by one contracting party is of such a nature that the other party may terminate their contractual relation before the expiry of its term (for example, "fundamental breach", "material breach" or similar expressions). Such situations are referred to in the *Guide* as "serious breach".

16. Circumscribing the possibility of termination to cases of serious breach may give assurance to lenders and project promoters that they will be protected against unreasonable or premature decisions by the contracting authority. The law may generally provide for the contracting authority's right to terminate the project agreement upon serious breach by the concessionaire and leave it for the project agreement to define further the notion of serious breach and, as appropriate, provide illustrative examples of it. From a practical point of view, it is not advisable to attempt, by statute or in the project agreement, to provide a list of the events that justify termination.

17. As a general rule, it is desirable that the concessionaire be granted an additional period of time to fulfil its obligations and to avert the consequences of its breach prior to the contracting authority's resorting to remedies. For example, the concessionaire should be given notice specifying the nature of the relevant circumstances and requiring it to rectify them within a certain period. The possibility might also be given for the lenders and sureties, as the case may be, to avert the consequences of the concessionaire's breach, for instance by temporarily engaging a third party to cure the consequences of breach by the concessionaire, in accordance with the terms of the performance bonds provided to the contracting authority or the terms of a direct agreement between the lenders and the contracting authority (see chap. IV, "Construction and operation of infrastructure", paras. 108-120 and 147-150). The project agreement may also provide that, if the circumstances are not rectified before the expiry of the

relevant period, the contracting authority may then terminate the project agreement, subject to first notifying the lenders and giving them an opportunity within a certain period to exercise any right of substitution that the lenders might have in accordance with a direct agreement between them and the contracting authority. However, reasonable deadlines need to be set, since the contracting authority cannot be expected to bear indefinitely the continuing cost of a situation of breach of the project agreement by the concessionaire. Furthermore, the procedures should be without prejudice to the contracting authority's right to step in to avert the risk of disruption of service by the concessionaire (see chap. IV, "Construction and operation of infrastructure", paras. 145 and 146).

(i) Serious breach before the beginning of construction

18. The concessionaire typically needs to accomplish a series of steps prior to undertaking construction works. Some of these requirements may even constitute conditions precedent to the entry into force of the project agreement. Examples of events that often justify the withdrawal of the concession award at an early stage include the following:

(a) Failure to secure the required financial means, to sign the project agreement or to establish the project company within the established deadline;

(b) Failure to obtain licences or permits required for pursuing the activity that is the object of the concession;

(c) Failure to undertake the construction of the facility, to commence development of the project or to submit the plans and designs required within a set period of time from the award of the concession.

19. Termination should in principle be reserved for situations where the contracting authority may no longer reasonably expect that the selected concessionaire will take the necessary measures to commence execution of the project. In that connection, it is important for the contracting authority to take into account any circumstances that may excuse the concessionaire's delay in fulfilling its obligations. Furthermore, the concessionaire should not suffer the consequences of inaction or error on the part of the contracting authority or other public authorities. For instance, the termination of the project agreement would not normally be justified if the concessionaire's failure to obtain government licences and permits within the agreed schedule was not attributable to the concessionaire's own fault.

(ii) Serious breach during the construction phase

20. Examples of events that may justify the termination of the project agreement during the construction phase include the following:

(a) Failure to observe building regulations, specifications or minimum design and performance standards and non-excusable failure to complete work within the agreed schedule;

(b) Failure to provide or renew the required guarantees in the agreed terms;

(c) Violation of essential statutory or contractual obligations.

21. Termination should be commensurate with the degree of breach by the concessionaire and the consequences of breach for the contracting authority. For instance, the contracting authority may have a legitimate interest in specifying a date when the construction must be completed and may therefore be justified in regarding a delay in completion as an event of breach and hence a ground for termination. However, delay alone, in particular if it is not excessive in relation to the specifications of the project agreement, might not be sufficient reason for termination when the contracting authority is otherwise satisfied of the

concessionaire's ability to complete the construction in accordance with the required quality standards and its commitment to doing so.

(iii) Serious breach during the operational phase

22. Examples of particular instances of breach that typically justify the termination of the concession during the operational phase include any of the following:

(a) Serious failure to provide services in accordance with the statutory and contractual standards of quality, including disregard of price control measures;

(b) Non-excusable suspension or interruption of the provision of the service without prior consent from the contracting authority;

(c) Serious failure by the concessionaire to maintain the facility, its equipment and appurtenances in accordance with the agreed standards of quality or non-excusable delay in carrying out maintenance works in accordance with the agreed plans, schedules and timetables;

(d) Failure to comply with sanctions imposed by the contracting authority or the regulatory agency, as appropriate, for infringements of the concessionaire's duties.

23. For the purpose of enhancing transparency and integrity in governmental matters, the laws of some countries also provide for the termination of project agreements if the concessionaire is guilty of tax fraud or other types of fraudulent acts, or if its agents or employees are involved in bribery of public officials and other corrupt practices (see also chap. VII, "Other relevant areas of law", paras. 50-52). The later considerations underscore the importance of designing effective mechanisms to combat corruption and bribery and to afford the concessionaire the opportunity to file complaints against demands for illegal payments or unlawful threats by officials of the host country.

(b) Insolvency of the concessionaire

24. Infrastructure services typically need to be provided continuously and for that reason most domestic laws stipulate that the agreement may be terminated if the concessionaire is declared insolvent or bankrupt. In order to ensure the continuity of the service, the assets and property required to be handed over to the contracting authority may be excluded from the insolvency proceedings and the law may require prior governmental approval for any act of disposition by a liquidator or insolvency administrator of any categories of assets owned by the concessionaire.

25. In legal systems that allow the establishment of security interests over the concession itself (see chap. IV, "Construction and operation of infrastructure", para. 57), the law usually provides that the contracting authority may, in consultation with the secured creditors, appoint a temporary administrator so as to ensure the continued provision of the relevant service, until the secured creditors admitted to the insolvency proceedings decide, upon the recommendation of the insolvency administrator, whether the activity should be pursued or whether the right to exploit the concession should be put to a bidding process.

(c) Termination for reasons of public interest

26. In the contracting practice of some countries, public authorities procuring construction works traditionally retain the right to terminate the construction contract for reasons of public interest (that is, without having to provide any justification other than that the termination is in the Government's interest). In some common law jurisdictions, that right, which is sometimes referred to as "termination for convenience", can only be exercised if expressly provided for in

a statute or in the relevant contract. Several legal systems belonging to the civil law tradition also recognize a similar power of public authorities to terminate contracts for reasons of public interest or "general interest". In some countries, such a right may be implied in the Government's contracting power, even in the absence of an explicit statutory or contractual provision to that effect. The Government's right to terminate for reasons of public interest, in those legal systems which recognize it, is regarded as essential in order to preserve the Government's unfettered ability to exercise its functions affecting the public good.

27. Nevertheless, the conditions for the exercise of this right, and the consequences of doing so, should be carefully considered. The authority to determine what constitutes public interest may lie within the Government's discretion, so that the contracting authority's decision to terminate the project agreement could only be challenged under specific circumstances (for instance, improper motive, "*détournement de pouvoir*"). However, a general and unqualified right to terminate the project agreement for reasons of public interest may represent an imponderable risk that neither the concessionaire nor the lenders may be ready to accept without sufficient guarantees that they will receive prompt compensation for the loss sustained. The possibility of termination for reasons of public interest, where contemplated, should therefore be made known to prospective investors on the earliest possible occasion and should be expressly mentioned in the draft project agreement circulated with the request for proposals (see chap. III, "Selection of the concessionaire", para. 67). The compensation due for termination for reasons of public interest may, in practice, cover items that are taken into account when calculating the compensation that is due for termination for serious breach by the contracting authority (see para. 42). Furthermore, it is generally advisable to limit the exercise of the right to terminate the project agreement to situations where such termination is needed for a compelling reason of public interest, which should be restrictively interpreted (for example, where major subsequent changes in governmental plans and policies require the integration of a project into a larger network or where changes in the contracting authority's plans require major project revisions that substantially affect the original design or the project's commercial feasibility under private operation). In particular, it is not advisable to regard the right of termination for reasons of public interest as a substitute for other contractual remedies in case of dissatisfaction with the concessionaire's performance (see chap. IV, "Construction and operation of infrastructure", paras. 140-150).

2. Termination by the concessionaire

28. While the contracting authority in some legal systems may retain an unqualified right to terminate the project agreement, the grounds for termination by the concessionaire are usually limited to serious breach by the contracting authority or other exceptional situations and do not normally include a general right to terminate the project agreement at will. Moreover, some legal systems do not recognize the concessionaire's right to terminate the project agreement unilaterally, but only the right to request a third party, such as the competent court, to declare the termination of the project agreement.

(a) Serious breach by the contracting authority

29. Generally, the concessionaire's right to terminate the project agreement is limited to situations where the contracting authority is found to be in breach of a substantial part of its obligations (such as failure to make agreed payments to the concessionaire or failure to issue licences required for the operation of the facility for reasons other than the concessionaire's own fault). In those legal systems where the contracting authority has the right to request modifications in the project, the concessionaire may have the right to terminate the project

agreement if the contracting authority alters or modifies the original project in such a fashion as to cause a substantial increase in the amount of investment required and the parties fail to agree on the appropriate amount of compensation (see chap. IV, "Construction and operation of infrastructure", paras. 73-76).

30. In addition to serious breach by the contracting authority itself, it may be equitable to authorize termination by the concessionaire should the latter be rendered unable to provide the service as a result of acts of public authorities other than the contracting authority, such as failure to provide certain measures of support required for the execution of the project agreement (see chap. II, "Project risks and government support", paras. 35-60).

31. Although termination by the concessionaire may not always require a final finding by a judicial or other dispute settlement body, there may be limits to the remedies available to the concessionaire in the event of breach by the contracting authority. Pursuant to a rule of law followed in many legal systems, a party to a contract may withhold performance of its obligations in the event of breach by the other party of a substantial part of its obligations. However, in some legal systems that rule does not apply to government contracts and the law provides instead that government contractors are not excused from performing solely on the ground of breach by the contracting authority unless and until the contract is rescinded by a judicial or arbitral decision.

32. Limitations on the concessionaire's right to withhold performance are typically intended to ensure the continuity of public services (see chap. IV, "Construction and operation of infrastructure", paras. 86 and 87). Nevertheless, it should be noted that while the contracting authority may mitigate the consequences of breach by the concessionaire by using its right to step in, the concessionaire does not usually have a comparable remedy. In the event of serious breach by the contracting authority, the concessionaire may sustain considerable or even irreparable damage, depending on the time required to obtain a final decision releasing the concessionaire from its obligations under the project agreement. These circumstances underscore the importance of government guarantees in respect of obligations assumed by contracting authorities (see chap. II, "Project risks and government support", paras. 45-50) and the need for allowing the parties the choice of expeditious and effective dispute settlement mechanisms (see chap. VI, "Settlement of disputes", paras. 3-42).

(b) Changes in conditions

33. Domestic laws often allow the concessionaire to terminate the project agreement if the concessionaire's performance has been rendered substantially more onerous by the occurrence of an unforeseen change in conditions and the parties have failed to agree on an appropriate revision to adapt the project agreement to the changed conditions (see chap. IV, "Construction and operation of infrastructure", paras. 126-130).

3. Termination by either party

(a) Impediment of performance

34. Some laws provide that the parties may terminate the project agreement if the performance of their obligations is rendered permanently impossible as a result of a circumstance defined in the project agreement as an exempting impediment (see chap. IV, "Construction and operation of infrastructure", paras. 132-139). In that connection, it is advisable to provide in the project agreement that if the exempting impediment persists for a certain period or if the cumulative duration of two or more exempting impediments exceeds a certain time, the agreement may be

terminated by either party. If the execution of the project is rendered impossible on legal grounds, because of changes in legislation or as a result of judicial decisions affecting the validity of the project agreement, for instance, such a termination right might not require any period of time to elapse and might be exercised immediately upon the change of legislation or other legal obstacle becoming effective.

(b) Mutual consent

35. Some domestic laws authorize the parties to terminate the project agreement by mutual consent, usually subject to the approval of a higher authority. Legislative power to this effect may be needed by the contracting authority in legal systems where the termination by mutual consent might amount to a discontinuation of the public service for which the contracting authority is responsible.

E. Consequences of expiry or termination of the project agreement

36. The concessionaire's right to operate the facility and to provide the relevant service typically finishes upon expiry of the project term or termination of the project agreement. Unless the infrastructure is to be permanently owned by the concessionaire, the expiry or termination of the project agreement often requires the transfer of assets to the contracting authority or to another concessionaire who undertakes to operate the facility. There may be important financial consequences that will need to be regulated in detail in the project agreement, in particular in the event of termination by either party. The parties will also need to agree on various wind-up measures to ensure the orderly transfer of the responsibility for operating the facility and providing the service.

1. Transfer of project-related assets

37. In most cases, the assets and property originally made available to the concessionaire and other goods related to the project are to revert to the contracting authority upon expiry or termination of the project agreement (see chap. IV, "Construction and operation of infrastructure", paras. 23-29). In a typical "build-operate-transfer" project, the concessionaire would also be obliged to transfer to the contracting authority the physical infrastructure and other project-related assets upon expiry or termination of the project agreement. The assets required to be transferred to the contracting authority often include intangible assets, such as outstanding receivables and other rights existing at the time of transfer. Depending on the project, the assets to be transferred may include specific technology or know-how (see paras. 51-55). It should be noted that in some projects the assets are transferred directly from the concessionaire to another concessionaire who succeeds it in the provision of the service.

(a) Transfer of assets to the contracting authority

38. Different arrangements may be needed, depending on the type of asset to be transferred (see chap. IV, "Construction and operation of infrastructure", para. 28):

(a) *Assets that must be transferred to the contracting authority*. In the legal tradition of some countries, at the end of the project term, the concessionaire is required to transfer such assets free of any liens and encumbrances and at no cost to the contracting authority, except for compensation for improvements made to, or modernization of, the property for the purpose of ensuring the continuity of the service the cost of which has not yet been recovered by the concessionaire. In practice, such a rule presupposes the negotiation of a concession period

sufficiently long and a level of revenue high enough for the concessionaire to amortize fully its investment and to repay its debts in full. Other laws allow for more flexibility by authorizing the contracting authority to compensate the concessionaire for the residual value, if any, of assets built by the concessionaire;

(b) *Assets that may be purchased by the contracting authority, at its option*. If the contracting authority decides to exercise its option to purchase those assets, the concessionaire is normally entitled to compensation corresponding to their fair market value at the time. However, if those assets were expected to be fully amortized (that is, if the concessionaire's financing arrangements do not envisage any expectation of residual value of the assets), then the price paid might be only nominal. In the contracting practice of some countries, it is usual for contracting authorities to be granted some security interest in such assets as a guarantee for their effective transfer;

(c) *Assets that remain the private property of the concessionaire*. Typically these assets may be freely removed or disposed of by the concessionaire.

(b) Transfer of assets to a new concessionaire

39. As indicated earlier, the contracting authority may wish to rebid the concession at the end of the project agreement, rather than to operate the facility itself (see para. 3). For that purpose, it may be useful for the law to require the concessionaire to make the assets available to a new concessionaire. In order to ensure an orderly transition and continuity of the service, the concessionaire should be required to cooperate with the new concessionaire in the handover. The transfer of assets between the concessionaires may require that some compensation be paid to the incumbent concessionaire, depending on whether or not the assets have been amortized.

40. One important element to consider in this connection is the structure of the financial proposal formulated by the concessionaire during the selection process (see also chap. IV, "Construction and operation of infrastructure", para. 27). In public infrastructure projects, one of the basic assumptions of the bidders' financial proposal is that all assets required to be built or acquired for the project will be fully amortized (that is, their cost will be recovered in full) in the life of the project. Thus, the financial proposals will not normally include an expectation of residual value for the assets at the end of the project period. In such cases, there may not be a prima facie reason for requiring a successor concessionaire to pay any compensation to the original concessionaire, which may be required to make all assets available to its successor at no cost or only for a nominal consideration. Indeed, if the concessionaire has achieved its expected return, a transfer payment from a successor concessionaire would be an additional cost that would ultimately have to be remunerated by the prices charged by the successor under the second agreement. However, if the tariff level contemplated in the concessionaire's original proposal was based on the assumption of some residual value of the assets at the end of the project period or if the financial proposal assumed significant revenue from third parties, the concessionaire might be entitled to compensation for assets handed over to a successor concessionaire.

(c) Condition of assets at the time of transfer

41. Where assets are handed over to the contracting authority or transferred directly to a new concessionaire upon the expiry of the concession period, the concessionaire is typically obligated to transfer them, free of liens or encumbrances, and in such condition as would be necessary for normal functioning of the infrastructure facility, taking into account the needs of

the service. The contracting authority's right to receive those assets in such operating condition is complemented in some laws by the obligation imposed upon the concessionaire to keep and transfer the project in such proper condition as prudent maintenance requires and to provide some sort of guarantee to that effect (see chap. IV, "Construction and operation of infrastructure", para. 118). Where the contracting authority requires the assets to be returned in a prescribed condition, the required conditions should be reasonable. While it may be reasonable for the contracting authority to require that the assets have some defined period of residual life, it would not be reasonable to expect them to be as new. Furthermore, these requirements may not be applicable in the event of termination of the project agreement, in particular termination prior to successful completion of the construction phase.

42. It is advisable to devise procedures for ascertaining the condition of the assets that should be transferred to the contracting authority. It may be useful, for example, to establish a committee comprised of representatives of both the contracting authority and the concessionaire to establish whether the facilities are in the prescribed condition and conform to the relevant requirements set forth in the project agreement. The project agreement may also provide for the appointment and terms of reference of such a committee, which may be given authority to request reasonable measures by the concessionaire to repair or eliminate any defects and deficiencies found in the facilities. It may be advisable to provide for a special inspection to take place one year prior to the termination of the concession, following which the contracting authority may require additional maintenance measures by the concessionaire so as to ensure that the goods are in proper condition at the time of the transfer. The contracting authority may wish to require that the concessionaire provide special guarantees for the satisfactory handover of the facilities (see chap. IV, "Construction and operation of infrastructure", para. 118). The contracting authority might draw on such guarantees to pay the repair cost of damaged assets or property.

2. Financial arrangements upon termination

43. Termination of the project agreement may occur before the concessionaire has been able to recover its investment, repay its debts and yield the expected profit, which may cause significant loss to the concessionaire. Loss may also be sustained by the contracting authority, which may need to make additional investment or incur considerable expense in order, for instance, to ensure the completion of the facility or the continued provision of the relevant services. In view of these circumstances, project agreements typically contain extensive provisions dealing with the financial rights and obligations of the parties upon termination. The usual standards of compensation typically vary according to the various grounds for termination. Nevertheless, the following factors are usually taken into account in compensation arrangements:

(a) *Outstanding debt, equity investment and anticipated profit.* Project termination is typically included among the events of default in the concessionaire's loan agreements. Since loan agreements usually include a so-called "acceleration clause", whereby the entire debt may become due upon the occurrence of an event of default, the immediate loss sustained by the concessionaire upon termination of the project agreement may include the amount of debt then outstanding. Whether and to what extent such a loss might be compensated for by the contracting authority usually depends on the grounds for terminating the project agreement. Partial compensation may be limited to an amount corresponding to the value of works satisfactorily performed by the concessionaire, whereas full compensation would cover the entire outstanding debt. Another category of loss that is sometimes taken into account in compensation arrangements refers to loss of equity investment by the project promoters, to the

extent that such an investment has not yet been recovered at the time of termination. Lastly, termination also deprives the concessionaire of future profits that the facility may generate. Although lost profits are not usually regarded as actual damage, in exceptional circumstances, such as wrongful termination by the contracting authority, the current value of expected future profit may be included in the compensation due to the concessionaire;

(b) *Degree of completion, residual value and amortization of assets.* Contractual compensation schemes for various termination grounds typically include compensation commensurate with the degree of completion of the works at the time of termination. The value of the works is usually determined on the basis of the investment required for construction (in particular if the termination takes place during the construction phase), the replacement cost or the "residual" value of the facility. The residual value means the market value of the infrastructure at the time of termination. Market value may be difficult to determine or even inexistent for certain types of physical infrastructure (such as bridges or roads) or for facilities whose operational life is close to expiry. Sometimes the residual value may be estimated taking into account the expected usefulness of the facility for the contracting authority. However, difficulties may be found in establishing the value of unfinished works, in particular if the amount of the investment still required by the contracting authority to render the facility operational would exceed the amount actually invested by the concessionaire. In any event, full payment of residual value seldom takes place, in particular where the project's revenue constitutes the sole remuneration for the concessionaire's investment. Thus, instead of full compensation for the facility's value, the concessionaire often receives compensation only for the residual value of assets that have not yet been fully amortized at the time of termination.

(a) Termination due to breach by the concessionaire

44. The concessionaire is not usually entitled to damages in the event of termination due to its own breach. In some cases the concessionaire may be under an obligation to pay damages to the contracting authority, although, in practice, a defaulting concessionaire whose debts are declared due by its creditors would seldom have sufficient financial means left for actual payment of such damages.

45. It should be noted that termination due to breach, even where it is regarded as a sanction for serious performance failures, should not result in the unjust enrichment of either party. Thus, termination does not necessarily entail a right for the contracting authority to take over assets without making any payment to the concessionaire. An equitable solution for dealing with this issue may be to distinguish between the different types of asset, according to the arrangements envisaged for them in the project agreement (see para. 38):

(a) *Assets that must be transferred to the contracting authority.* Where the project agreement requires the automatic transfer of project assets to the contracting authority at the end of the project agreement, termination on breach does not usually entail the payment of compensation to the concessionaire for those assets, except for the residual value of work satisfactorily performed, to the extent that it has not yet been amortized by the concessionaire;

(b) *Assets that may be purchased by the contracting authority, at its option.* Financial compensation may be adequate in cases where the contracting authority has an option to buy the assets at market value on expiry of the project agreement or the right to require that such an option be given to the winner of a new project award. However, it may be legitimate to envisage a financial compensation that is less than the full value of the assets so as to stimulate performance by the concessionaire. By the same token, such compensation may not need to cover the full cost of repaying the concessionaire's outstanding debt. It is advisable to set forth

the details of the formula for financial compensation in the project agreement (that is, whether it covers the break-up value of the asset or the lesser of the outstanding debt and the alternative use value);

(c) *Assets that remain the private property of the concessionaire.* Assets in the concessionaire's private property that do not fall under (a) or (b) above may usually be removed and disposed of by the concessionaire, so that the need for compensation arrangements seldom arises. However, a different situation may arise in the case of fully privatized projects, where all assets, including those essential for the provision of the services, are owned by the concessionaire. In such cases, in order to ensure the continuity of the services, the contracting authority may find it necessary to take over the assets, even though not contemplated in the project agreement. In such cases, it would be equitable to compensate the concessionaire for the fair market value of the assets. The project agreement may, however, provide that the compensation should be reduced by the costs incurred by the contracting authority in operating the facility or engaging another operator.

(b) Termination due to breach by the contracting authority

46. The concessionaire is usually entitled to full compensation for loss sustained as a result of termination on grounds attributable to the contracting authority. The compensation due to the concessionaire usually includes compensation for the value of the works and installations, to the extent they have not already been amortized, as well as for the loss caused to the concessionaire, including lost profits, which are usually calculated on the basis of the concessionaire's revenue during previous financial years, when termination occurs during the operational phase, or are based on a projection of the expected benefit during the duration originally envisaged. The concessionaire may be entitled to full compensation of debt and equity, including debt service and lost profits.

(c) Termination on other grounds

47. When considering compensation arrangements for termination due to circumstances unrelated to breach by either party, it may be useful to distinguish exempting impediments from termination declared by the contracting authority for reasons such as public interest or other similar reasons.

(i) Termination due to exempting impediments

48. By definition, exempting impediments are events beyond the parties' control and, as a general rule, termination under such circumstances might not give rise to claims for damages by either party. However, there may be circumstances where it might be equitable to provide for some compensation to the concessionaire, such as fair compensation for works already completed, in particular where, because of the specialized nature of the assets, they cannot be removed by the concessionaire or meaningfully used by it, but may be effectively used by the contracting authority for the purpose of providing the relevant service (a bridge, for instance). However, since termination in such cases cannot be attributed to the contracting authority, the compensation due to the concessionaire may not necessarily need to be "full" compensation (that is, repayment of debt, equity and lost profits).

(ii) Termination for convenience

49. Where the project agreement recognizes the contracting authority's right to terminate for its convenience, the compensation payable to the concessionaire usually covers compensation

for the same items included in compensation payable upon termination for breach by the contracting authority (see para. 46), although not necessarily to the full extent. In order to establish the equitable amount of compensation due to the concessionaire, it may be useful to distinguish between termination for convenience during the construction phase and termination for convenience during the operational phase:

(a) *Termination for convenience during the construction phase*. If the project agreement is terminated during the construction phase, the compensation arrangements may be similar to those which are followed in connection with large construction contracts that allow for termination for convenience. In those cases, the contractor is usually entitled to the portion of the price that is attributable to the construction satisfactorily performed, as well as for expenses and losses incurred by the contractor arising from the termination. However, since the contracting authority does not normally pay a price for the construction work carried out by the concessionaire, the main criterion for calculating compensation would typically be the total investment effectively made by the concessionaire up to the time of termination, including all sums actually disbursed under the loan facilities extended by the lenders to the concessionaire for the purpose of carrying out construction under the project agreement, and expenses related to the cancellation of loan agreements. One additional question is whether and to what extent the concessionaire may be entitled to recover lost profit for the portion of the contract that has been terminated for convenience. On the one hand, the concessionaire might have foregone other business opportunities in anticipation of completing the project and operating the facility through the anticipated duration of the concession. On the other hand, an obligation of the contracting authority to compensate the concessionaire for its lost profit might make it financially prohibitive for the contracting authority to exercise its right of termination for convenience. One approach may be for the project agreement to establish a scale of payments to be made by the contracting authority as compensation for lost profits and the amount of the payments depending upon the stage of the construction that has been completed when the project agreement is terminated for convenience;

(b) *Termination for convenience during the operational phase*. As regards the construction work satisfactorily completed by the concessionaire, the compensation arrangements may be the same as for termination for convenience during the construction phase. However, equitable compensation for termination for convenience during the operational phase might require fair compensation for lost profits. The higher standard of compensation in this case may be justified by the fact that, unlike termination during the construction phase, when the contracting authority might need to undertake to complete the work at its own expense, upon termination during the operational phase the contracting authority might be able to receive a completed facility capable of being operated profitably. Compensation for lost profits is often calculated on the basis of the concessionaire's revenue during a certain number of previous financial years, but in some cases other elements, such as the anticipated profit on the basis of the agreed tariffs, may need to be taken into account. This is so because in some infrastructure projects such as toll roads and similar projects, which are characterized by high financial costs and relatively low income at the early stages of operation, termination may occur before the project has a history of profitability.

3. Wind-up and transitional measures

50. Where the facility is transferred to the contracting authority at the end of the concession period, the parties may need to make a series of arrangements in order to ensure that the contracting authority will be able to operate the facility at the prescribed standards of efficiency and safety. The project agreement may provide for the concessionaire's obligation to transfer

certain technology or know-how required to operate the infrastructure facility. The project agreement may also provide for the continuation, for a certain transitional period, of certain obligations of the concessionaire in respect of the operation and maintenance of the facility. It may further include an obligation, on the part of the concessionaire, to supply or facilitate the supply of spare parts that may be needed by the contracting authority to carry out repairs in the facility. It should be noted, however, that the concessionaire might not be in a position to undertake itself some of the transitional measures referred to below, since in most cases the concessionaire would have been established for the sole purpose of carrying out the project and would need to procure the relevant technology or spare parts from third parties.

(a) Transfer of technology

51. In some cases, the facility transferred to the contracting authority will embody various technological processes necessary for the generation of certain goods, such as electricity or potable water, or the provision of the relevant services, such as telephone services. The contracting authority will often wish to acquire a knowledge of those processes and their application. The contracting authority will also wish to acquire the technical information and skills necessary for the operation and maintenance of the facility. Even where the contracting authority has the basic capability to undertake certain elements of the operation and maintenance (for example, building or civil engineering), the contracting authority may need to acquire a knowledge of special technical processes necessary to effect the operation in a manner appropriate to the facility in question. The communication to the contracting authority of that knowledge, information and skills is often referred to as the "transfer of technology". Obligations concerning the transfer of technology cannot be unilaterally imposed on the concessionaire and, in practice, these matters are the subject of extensive negotiations between the parties concerned. While the host country has a legitimate interest in gaining access to the technology needed to operate the facility, due account should be taken of the commercial interests and business strategies of the private investors.

52. Differing contractual arrangements can be adopted for the transfer of technology and the performance of the other obligations necessary to construct and operate the facility. The transfer of technology itself may occur in different ways, for example, through the licensing of industrial property, through the creation of a joint venture between the parties or the supply of confidential know-how. The *Guide* does not attempt to deal comprehensively with contract negotiation and drafting relating to the licensing of industrial property or the supply of know-how, as this subject has already been dealt with in detail in publications issued by other United Nations bodies.[1] The following paragraphs merely note certain major issues concerning the communication of skills necessary for the operation and maintenance of the facility through the training of the contracting authority's personnel or through documentation.

53. The most important method of conveying to the contracting authority the technical information and skills necessary for the proper operation and maintenance of the works is the training of the contracting authority's personnel. In order to enable the contracting authority to decide on its training requirements, in the request for proposals or during the contract negotiations the contracting authority might request the concessionaire to supply the contracting authority with an organizational chart showing the personnel requirements for the operation and maintenance of the works, including the basic technical and other qualifications the personnel must possess. Such a statement of requirements should be sufficiently detailed to enable the contracting authority to determine the extent of training required in relation to the personnel available to it. The concessionaire will often have the capability to provide the

training. In some cases, however, the training may be given more effectively by a consulting engineer or through an institution specializing in training.

54. Technical information and skills necessary for the proper operation and maintenance of the facility may also be conveyed through the supply of technical documentation. The documentation to be supplied may consist of plans, drawings, formulae, manuals of operation and maintenance and safety instructions. It may be advisable to list in the project agreement the documents to be supplied. The concessionaire may be required to supply documents that are comprehensive and clearly drafted and are in a specified language. It may be advisable to obligate the concessionaire, at the request of the contracting authority, to give demonstrations of procedures described in the documentation if the procedures cannot be understood without demonstrations.

55. The points in time when the documentation is to be supplied may be specified. The project agreement may provide that the supply of all documentation is to be completed by the time fixed in the contract for completion of the construction. The parties may also wish to provide that transfer of the facility is not to be considered completed unless all documentation relating to the operation of the works and required under the contract to be delivered prior to the completion has been supplied. It may be advisable to provide that some documentation, such as operating manuals, is to be supplied during the course of construction, as such documentation may enable the contracting authority's personnel or engineer to obtain an understanding of the working of machinery or equipment while it is being erected.

(b) Assistance in connection with operation and maintenance of the facility after its transfer

56. The degree of assistance from the concessionaire needed by the contracting authority with regard to the supply of spare parts and services will depend on the technology and skilled personnel available to the contracting authority. If the contracting authority lacks personnel sufficiently skilled for the technical operation of the facility, it may wish to obtain the concessionaire's assistance in operating the facility, at least for an initial period. The contracting authority may, in some cases, wish the concessionaire to provide the personnel to occupy many of the technical posts in the facility, while in other cases the contracting authority may wish the concessionaire only to provide technical experts to collaborate in an advisory capacity with the contracting authority's personnel in the performance of a few highly specialized operations.

57. In order to assist the contracting authority in operating and maintaining the facility, the project agreement may obligate the concessionaire to submit, prior to the transfer of the facility, an operation and maintenance programme designed to keep the facility operating over its remaining lifetime at the level of efficiency required under the project agreement. An operation and maintenance programme would include matters such as an organizational chart showing the key personnel required for the technical operation of the facility and the functions to be discharged by each person; periodic inspection of the facility; lubrication, cleaning and adjustment; and replacement of defective or worn-out parts. Maintenance may also include operations of an organizational character, such as establishing a maintenance schedule or maintenance records. The concessionaire may also be required by the contracting authority to supply operation and maintenance manuals setting out appropriate operation and maintenance procedures. Those manuals should be in a format and language readily understood by the contracting authority's personnel.

58. An effective means of training the contracting authority's personnel in operation and maintenance procedures may be to provide in the project agreement that the personnel of the

contracting authority are to be associated with the personnel of the concessionaire in carrying out the operation and maintenance for a certain time prior to or beyond the transfer of the facility. The positions to be occupied by the personnel employed by the contracting authority can then be identified and their qualifications and experience specified. In order to avoid friction and inefficiency, it is desirable that any authority to be exercised by the personnel of each party over the personnel of the other during the relevant period be clearly described.

(c) Supplies of spare parts

59. In projects that provide for the transfer of the facility to the contracting authority, the contracting authority will have to obtain spare parts to replace those which are worn out or damaged and to maintain, repair and operate the facility. Spare parts may not be available locally and the contracting authority may have to depend on the concessionaire to supply them. The planning of the parties with respect to the supply of spare parts and services after the transfer of the facility would be greatly facilitated if the parties were to anticipate and provide in the project agreement for the needs of the contracting authority in that regard. However, given the long duration of most infrastructure projects, it may be difficult for the parties to anticipate and provide in the project agreement for the needs of the contracting authority after the transfer of the facility.

60. A possible approach may be for the parties to enter into a separate contract regulating these matters.[2] Such a contract may be entered into closer in time to the transfer of the facility, when the contracting authority may have a clearer view of its requirements. If spare parts are manufactured not by the concessionaire but for the concessionaire by suppliers, the contracting authority may prefer to enter into contracts with those suppliers rather than to obtain them from the concessionaire or, alternatively, the contracting authority may wish to have the concessionaire procure them as the contracting authority's agent.

61. It is desirable for the contracting authority's personnel to develop the technical capacity to install the spare parts. For this purpose, the project agreement may obligate the concessionaire to supply the necessary instruction manuals, tools and equipment. The instruction manuals should be in a format and language readily understood by the contracting authority's personnel. The contract may also require the concessionaire to furnish "as built" drawings indicating how the various pieces of equipment interconnect and how access can be obtained to them to enable the spare parts to be installed and to enable maintenance and repairs to be carried out. In certain cases, it may be appropriate for the concessionaire to be required to train the contracting authority's personnel in the installation of spare parts.

(d) Repairs

62. It is in the contracting authority's interest to enter into contractual arrangements that will ensure that the facility will be repaired expeditiously in the event of a breakdown. In many cases, the concessionaire may be better qualified than a third person to effect repairs. In addition, if the project agreement prevents the contracting authority from disclosing to third persons the technology supplied by the concessionaire, this may limit the selection of third persons to effect repairs to those who provide assurances regarding non-disclosure of the concessionaire's technology that are acceptable to the concessionaire. On the other hand, if major items of equipment have been manufactured for the concessionaire by suppliers, the contracting authority may find it preferable to enter into independent contracts for repair with them. In defining the nature and duration of repair obligations imposed on the concessionaire, if any, it is advisable to do so clearly and to distinguish them from obligations assumed by the concessionaire under quality guarantees to remedy defects in the facility.

Notes

[1] The negotiation and drafting of contracts for the licensing of industrial property and the supply of know-how is dealt with in detail in World Intellectual Property Organization, *Licensing Guide for Developing Countries* (WIPO publication No. 620 (E), 1977). The main issues to be considered in negotiating and drafting such contracts are set forth in the *Guidelines for Evaluation of Transfer of Technology Agreements*, Development and Transfer of Technology Series, No. 12 (ID/233, 1979), and in the *Guide for Use in Drawing Up Contracts Relating to the International Transfer of Know-How in the Engineering Industry* (United Nations publication, Sales No. E.70.II.E.15). Another relevant publication is the *Handbook on the Acquisition of Technology by Developing Countries* (United Nations publication, Sales No. E.78.II.D.15). For a discussion of transfer of technology in the context of contracts for the construction of industrial works, see the *UNCITRAL Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works* (United Nations publication, Sales No. E.87.V.10), chap. VI, "Transfer of technology".

[2] The Economic Commission for Europe has prepared a *Guide on Drawing Up International Contracts for Services Relating to Maintenance, Repair and Operation of Industrial and Other Works*, which may, *mutatis mutandis*, assist parties in drafting a separate contract or contracts dealing with maintenance and repair of the facility after its transfer to the contracting authority (ECE/TRADE/154).

United Nations A/CN.9/471/Add.7

General Assembly

Distr.: General
8 February 2000

Original: English

United Nations Commission on International Trade Law
Thirty-third session
New York, 12 June-7 July 2000

Privately financed infrastructure projects: draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

VI. Settlement of disputes

Contents

		Paragraphs	Page
Legislative recommendations			2
Notes on the legislative recommendations			2
A.	General remarks	1-2	2
B.	Disputes between the contracting authority and the concessionaire	3-42	3
1.	General considerations on methods for prevention and settlement of disputes	5-9	4
2.	Commonly used methods for preventing and settling disputes	10-42	5
C.	Disputes between the concessionaire and its lenders, contractors and suppliers	43	14
D.	Disputes between the concessionaire and its customers	44-46	14

V.00-50879 (E)

Legislative recommendations

Disputes between the contracting authority and the concessionaire (see paras. 3-42)

Recommendation 68. The contracting authority should be free to agree to dispute settlement mechanisms regarded by the parties as suited to the needs of the project, including arbitration.

[*Recommendation 68* bis. The law should indicate whether and, if so, to what extent the contracting authority may raise a plea of sovereign immunity, both as a bar to the commencement of arbitral or judicial proceedings as well as a defence against enforcement of the award or judgement.]

Disputes between the concessionaire and its lenders, contractors and suppliers (see para. 43)

Recommendation 69. The concessionaire And the project promoters should be free to choose the appropriate mechanisms for settling commercial disputes among project promoters or disputes between the concessionaire and its lenders, contractors, suppliers and other business partners.

Disputes between the concessionaire and its customers (see paras. 44-46)

Recommendation 70. The concessionaire may be required to make available simplified and efficient mechanisms for handling claims submitted by its customers or users of the infrastructure facility.

Notes on the legislative recommendations

A. General remarks

1. An important factor for the implementation of privately financed infrastructure projects is the legal framework in the host country for the settlement of disputes. Investors, contractors and lenders will be encouraged to participate in projects in countries where they have the confidence that any disputes arising out of contracts forming part of the project will be resolved fairly and efficiently. By the same token, efficient procedures for avoiding disputes or settling them expeditiously will facilitate the exercise of the contracting authority's monitoring functions and reduce the contracting authority's overall administrative cost. In order to create a more hospitable climate for investors, the legal framework of the host country should give effect to certain basic principles, such as the following: foreign firms should be guaranteed access to the courts under substantially the same conditions as domestic ones; parties to private contracts should have the right to choose foreign law as the law applicable to their contracts; foreign judgments should be enforceable; and there should be neither unnecessary restrictions to access to non-judicial dispute settlement mechanisms nor legal impediments for the creation of facilities for settling disputes amicably outside the judicial system.

2. Privately financed infrastructure projects typically require the establishment of a network of interrelated contracts and other legal relationships involving various parties. Legislative

provisions dealing with the settlement of disputes arising in the context of these projects must take account of the diversity of relations, which may call for different dispute settlement methods depending on the type of dispute and the parties involved. The main disputes may be divided into three broad categories:

(a) *Disputes arising under agreements between the concessionaire and the contracting authority and other governmental agencies*. In most civil law countries, the project agreement is governed by administrative law (see chap. VII, "Other relevant areas of law", paras. 24-27), while in other countries the agreement is in principle governed by contract law as supplemented by special provisions developed for government contracts for the provision of public services. This regime may have implications for the dispute settlement mechanism that the parties to the project agreement may be able to agree upon. Similar considerations may also apply to certain contracts entered into between the concessionaire and governmental agencies or government-owned companies supplying goods or services to the project or purchasing goods or services generated by the infrastructure facility;

(b) *Disputes arising under contracts and agreements entered into by the project promoters or the concessionaire with related parties for the implementation of the project*. These contracts usually include at least the following: (i) contracts between parties holding equity in the project company (e.g. shareholders' agreements, agreements regarding the provision of additional financing or arrangements regarding voting rights); (ii) financing and related agreements, which involve, apart from the project company, parties such as commercial banks, governmental lending institutions, international lending institutions and export credit insurers; (iii) contracts between the project company and contractors, which themselves may be consortia of contractors, equipment suppliers and providers of services; (iv) contracts between the project company and the parties who operate and maintain the project facility; and (v) contracts between the concessionaire and private companies for the supply of goods and services needed for the operation and maintenance of the facility;

(c) *Disputes between the concessionaire and other parties*. These other parties include the users or customers of the facility. These users may be, for example, a government-owned utility company that purchases electricity or water from the project company so as to resell it to the ultimate users; commercial companies, such as airlines or shipping lines contracting for the use of the airport or port; or individual persons paying for the use of a toll road. The parties to these disputes may not necessarily be bound by any prior legal relationship of a contractual or similar nature.

B. Disputes between the contracting authority and the concessionaire

3. Disputes that arise under the project agreement frequently involve problems that do not often arise in connection with other types of contracts. This is due to the complexity of infrastructure projects and the fact that they are to be performed over a long period of time, with a number of enterprises participating in the construction and in the operational phases. In addition, disputes under project agreements may concern highly technical matters connected with the construction processes, the technology incorporated in the works and the conditions for operating the facility. Furthermore, these projects usually involve governmental agencies and a high level of public interest. These circumstances place emphasis on the need to have mechanisms in place that avoid as much as possible the escalation of disagreements between the parties and preserve their business relationship; that prevent the disruption of the

construction works or the provision of the services; and that are tailored to the particular characteristics of the disputes that may arise.

4. Some of the main considerations particular to the various phases of implementation of privately financed infrastructure projects are discussed in this section. The settlement of the concessionaire's grievances in connection with decisions by regulatory agencies has been considered in the context of the authority to regulate infrastructure services (see chap. I, "General legislative and institutional framework", paras. 51-53). The settlement of disputes arising during the process of selecting a concessionaire (that is, pre-contractual disputes) has also been dealt with earlier in the Guide (see chap. III, "Selection of the concessionaire", paras. 118-122).

1. General considerations on methods for prevention and settlement of disputes

5. The issues that most frequently give rise to disputes during the life of the project agreement are those related to possible breaches of the agreement during the construction phase, the operation of the infrastructure facility or in connection with the expiry or termination of the project agreement. These disputes may be very complex and they often involve highly technical matters that need to be resolved speedily in order not to disrupt the construction or the operation of the infrastructure facility. For these reasons it is advisable for the parties to devise mechanisms that allow for the choice of competent experts to assist in the settlement of disputes. Furthermore, the long duration of privately financed infrastructure projects makes it important to devise mechanisms to prevent, as much as possible, disputes from arising so as to preserve the business relationship between the parties.

6. With a view to achieving the objectives mentioned above, project agreements often provide for composite dispute-settlement clauses designed to prevent, to the extent possible, disputes from arising, to foster reaching agreed solutions and to put in place efficient dispute settlement methods when disputes nevertheless arise. Such clauses typically provide for a sequential series of steps starting with an early warning of issues that may develop into a dispute unless the parties take action to prevent them. When a dispute does occur it is provided that the parties should exchange information and discuss the dispute with a view to identifying a solution. If the parties are unable to resolve the dispute themselves, then either party may require participation of an independent and impartial third party to assist them to find an acceptable solution. In most cases, adversarial dispute settlement mechanisms are only used when the disputes cannot be settled through the use of such conciliatory methods.

7. However, there may be limits to the parties' freedom to agree to certain dispute prevention or dispute settlement methods: one such limit may arise from the subject matter of the dispute; another limit may in some legal systems arise from the governmental character of the contracting authority. In some legal systems, the traditional position has been that the Government and its agencies may not agree on certain dispute settlement methods, in particular, arbitration. This position has often been restricted to mean that it does not apply to public enterprises of industrial or commercial character, which, in their relations with third parties, act pursuant to private law or commercial law.

8. Limitations to the freedom to agree on dispute settlement methods, including arbitration, may also relate to the legal nature of the project agreement. Under some civil law systems, project agreements may be regarded as administrative contracts, with the consequence that disputes arising thereunder need to be settled through the judiciary or through administrative courts of the host country. Under other legal systems, similar prohibitions may be expressly

included in legislation or judicial precedents directly applicable to project agreements, or may be the result of established contract practices, usually based on legislative rules or regulations.

9. For countries that wish to allow the use of non-judicial methods, including arbitration, for the settlement of disputes arising in connection with privately financed infrastructure projects, it is important to remove possible legal obstacles and to provide a clear authorization for domestic contracting authorities to agree on dispute settlement methods. The absence of such legislative authority may give rise to questions as to the validity of the dispute-settlement clause and cause delay in the settlement of disputes. If, for example, an arbitral tribunal finds that the arbitration agreement has been validly concluded despite any subsequent defence that the contracting authority had no authorization to conclude it, the question may reappear at the recognition and enforcement stage before a court in the host country or before a court of a third country where the award is to be recognized or enforced.

2. Commonly used methods for preventing and settling disputes

10. The following paragraphs set out the essential features of methods used for preventing and settling disputes and consider their suitability for the various phases of large infrastructure projects, namely, the construction phase, the operational phase and the post-termination phase. Although the project agreement usually provides for composite dispute prevention and dispute settlement mechanisms, care should be taken to avoid excessively complex procedures or to impose too many layers of different procedures. The brief presentation of selected methods for dispute prevention and dispute settlement methods contained in the following paragraphs is intended to inform legislators about the particular features and usefulness of these various methods. It should not be understood as a recommendation for the use of any particular combination of methods.

(a) Early warning

11. Early warning provisions may be an important tool to avoid disputes. Under these provisions, if one of the parties to a contract feels that events that have occurred, or claims that the party intends to make, have the potential to cause disputes, these events or claims should be brought to the attention of the other party as soon as possible. Delays in making these claims are not only a source of conflict, because they are likely to surprise the other party and therefore create resentment and hostility, but they also render the claims more difficult to prove. For that reason, early warning provisions typically require the claiming party to submit a quantified claim, along with the necessary proof, within an established time period. To make the provision effective, a sanction is frequently included for non-compliance with the provision, such as the loss of the right to pursue the claim or an increased burden of proof. In infrastructure projects, early warning frequently refers to events that might adversely affect the quality of the works or the public services, increase their cost, cause delays or endanger the continuity of the service. Early warning provisions are therefore useful throughout the duration of an infrastructure project.

(b) Partnering

12. Another tool that is used as a means of dispute avoidance is partnering. The object of partnering is to create, through mutually developed formal strategies and from the outset of a project, an environment of trust, teamwork and cooperation among all key parties involved in the project. Partnering has been found to be useful to avoid disputes and to commit the parties to work efficiently to achieve the goals of the project. The partnering relationships are defined in workshops attended by the key parties to the project, and usually organized by the

contracting authority. At the initial workshop, a mutual understanding of the concept of partnering is established, goals for the project for all the parties are defined and a procedure to resolve critical issues quickly is developed. At the conclusion of this workshop, a "partnering charter" is drafted and signed by the participants, signifying their commitment to work jointly towards the success of the project. The charter usually includes an issue resolution procedure designed to determine claims and resolve other problems, beginning at the lowest possible level of management and at the earliest possible opportunity. If a solution is not reached within a given time- frame, the issue is raised to the next level of management. Outsiders to the project are only called in if no agreement by the people responsible for the project is achieved.

(c) Facilitated negotiation

13. The purpose of this procedure is to aid the parties in the negotiation process. The parties appoint a facilitator at the commencement of the project. His function is to assist the parties in resolving any disputes, without providing subjective opinions on the issues, but rather coaxing them into analysing thoroughly the merits of their cases. This procedure is specially useful when there are numerous parties involved who would find it difficult to negotiate and coordinate all the differing opinions without such facilitation.

(d) Mediation and conciliation

14. The term "conciliation" is used in the Guide as a broad notion referring to proceedings in which a person or a panel assists the parties in an independent and impartial manner in their attempt to reach an amicable settlement of their dispute. Conciliation differs from negotiations between the parties in dispute (in which the parties would typically engage after the dispute has arisen) in that conciliation involves independent and impartial assistance to settle the dispute, whereas in settlement negotiations between the parties no third-person assistance is involved. The difference between conciliation and arbitration is that conciliation ends either in the settlement of the dispute agreed by the parties or it ends unsuccessfully; in arbitration, however, the arbitral tribunal imposes a binding decision on the parties, unless they have settled the dispute before the award is made. In practice, such conciliation proceedings are referred to by various expressions, including "mediation". Nevertheless, in the legal tradition of some countries, a distinction is drawn between conciliation and mediation to emphasize the fact that, in conciliation, a third party is trying to bring together the disputing parties to help them reconcile their differences, while mediation goes further by allowing the mediator to suggest terms for the resolution of the dispute. However, the terms "conciliation" and "mediation" are used as synonyms more frequently than not.

15. Conciliation is increasingly being increasingly practised in various parts of the world, including in regions where it was not commonly used in the past. This trend is reflected, inter alia, in the establishment of a number of private and public bodies offering conciliation services to interested parties. The conciliation procedure is usually private, confidential, informal and easily pursued. It may also be quick and inexpensive. The conciliator may assume multiple roles and is in general more active than a facilitator. He or she may frequently challenge the parties' position to stress weaknesses that usually facilitate agreement and, if authorized, may suggest possible settlement scenarios. The procedure is generally non-binding and the conciliator's responsibility is to facilitate settlement by directing the parties' attention to the issues and possible solutions, rather than passing judgement. This procedure is particularly useful when there are many parties involved and it would therefore be difficult to achieve an agreement by direct negotiations.

16. If the parties provide for conciliation in the project agreement, they will have to settle a number of procedural questions in order to increase the chance of a settlement. Settling such procedural questions is greatly facilitated by the incorporation into the contract, by reference, of a set of conciliation rules such as the UNCITRAL Conciliation Rules.[1] Other sets of conciliation rules have been prepared by various international and national organizations.

(e) Non-binding expert appraisal

17. This is a procedure where a neutral third party is charged with providing an appraisal on the merits of the dispute and suggested outcome. It serves as a "reality check" showing the contesting parties what the possible outcome of the more expensive and usually slower binding procedures such as arbitration or court proceedings would be. This procedure is useful where the parties have difficulty in communicating because their positions have become entrenched or where they do not see clearly the weaknesses of their positions or the strengths of the other party's positions. A non-binding expert appraisal is usually followed by negotiations, either direct or facilitated.

(f) Mini-trial

18. This procedure assumes the form of a mock trial in which site-level personnel of each party make submissions to a "tribunal" composed of a senior executive of each party and a third neutral person. After the submissions, which are typically to be made within predetermined time periods, the executives enter into a facilitated negotiation procedure with the assistance of a neutral person, to try to reach an agreement taking advantage of the issues that have been elucidated during the "trial". Counsel for the parties are frequently present and are useful in identifying the relevant issues. The purpose of the mini-trial is to inform senior executives of the issues involved in the dispute and to serve as a reality check of what the outcome of a real trial might be.

(g) Senior executive appraisal

19. This procedure is similar to the mini-trial but it is less adversarial and uses a more consensus-oriented approach. The procedure begins with the presentation of short position papers by each party, followed by short responses. At an "appraisal conference" headed by a facilitator, a senior executive from each of the parties makes brief oral presentations elucidating the issues submitted in the position papers or other points raised by the parties or the facilitator. This conference is followed by a negotiation meeting, chaired by the facilitator, with a view to reaching an agreement. Both the mini-trial and the senior executive appraisal tend to be less of a strong reality check than the non-binding expert appraisal and therefore less likely to motivate difficult decisions in the absence of commercial pressure to do so.

(h) Review of technical disputes by independent experts

20. During the construction phase, the parties may wish to consider providing for certain types of disputes to be referred to an independent expert appointed by both parties. This method may be of particular use in connection with disagreements relating to technical aspects of the construction of the infrastructure facility (for example, whether the works comply with contractual specifications or technical standards).

21. The parties may, for instance, appoint a design inspector or a supervisor engineer, respectively, to review disagreements relating to the inspection and approval of the design, and the progress of construction works (see chap. IV, "Construction and operation of

infrastructure", paras. 69-79). The independent experts should have expertise in the designing and construction of similar projects. The powers of the independent expert (such as whether the independent expert makes recommendations or issues binding decisions), as well as the circumstances under which the independent expert's advice or decision may be sought by the parties, should be set forth in the project agreement. In some large infrastructure projects, for instance, the advice of the independent expert may be sought by the concessionaire whenever there is a disagreement between the concessionaire and the contracting authority as to whether certain aspects of the design or construction works conform with the applicable specifications or contractual obligations. Referral of a matter to a design inspector or to a supervising engineer, as appropriate, may be particularly relevant in connection with provisions in the project agreement that require prior consent of the contracting authority for certain actions by the concessionaire, such as final authorization for operation of the infrastructure facility (see chap. IV, "Construction and operation of infrastructure", para. 78).

22. Independent experts have been often used for the settlement of technical disputes under construction contracts, and the various mechanisms and procedures developed in the practice of the construction industry may be used, mutatis mutandis, in connection with privately financed infrastructure projects. However, it should be noted that the scope of disputes between the contracting authority and the concessionaire is not necessarily the same as would be the case for disputes that typically arise under a construction contract. This is so because the respective positions of the contracting authority and the concessionaire under the project agreement are not fully comparable with those of the owner and the performer of works under a construction contract. For instance, disputes concerning the amount of payment due to the contractor for the quantities of works actually performed, which are frequent in construction contracts, are not typical for the relations between contracting authority and concessionaire, since the latter does not usually receive payments from the contracting authority for the construction works performed.

(i) Dispute review boards

23. Project agreements for large infrastructure projects often establish permanent boards composed of experts appointed by both parties, possibly with the assistance of an appointing authority, for the purpose of assisting in the settlement of disputes that may arise during the construction and the operational phases (referred to in the *Guide* as "dispute review boards"). Proceedings before a dispute review board can be informal and expeditious, and tailored to suit the characteristics of the dispute that it is called upon to settle. The appointment of a dispute review board may prevent misunderstandings or differences between the parties from developing into formal disputes that would require settlement in arbitral or judicial proceedings. In fact, its effectiveness as a tool for avoiding disputes is one of the special strengths of this procedure, but a dispute review board may also serve as a mechanism to resolve disputes, in particular when the board is given the power to render binding decisions.

24. Under the dispute review board procedure, the parties typically select, at the outset of the project, three experts renowned for their knowledge in the field of the project to constitute the board. These experts may be replaced if the project comprises different stages that may require different expertise (that is, different expertise will be required during the construction of the facility from during the later administration of the public service), and in some large infrastructure projects more than one board has been established. For example, one dispute review board may deal exclusively with disputes regarding matters of a technical nature (e.g. engineering design, fitness of certain technology, compliance with environmental standards) whereas another board may deal with disputes of a contractual or financial nature (regarding,

for instance, the amount of compensation due for delay in issuing licences or disagreements on the application of price adjustment formulas). Each board member should be experienced in the particular type of project, including experience in the interpretation and administration of project agreements, and should undertake to remain impartial and independent of the parties. These persons may be furnished with periodic reports on the progress of construction or on the operation of the infrastructure facility, as appropriate, and may be informed immediately of differences arising between the parties. They may meet with the parties, either at regular intervals or when the need arises, to consider differences that have arisen and to suggest possible ways of resolving those differences.

25. In their capacity as agents to avert disputes, the members of the board may make periodic visits to the project site, meet with the parties and keep informed of the progress of the work. These meetings help identify any potential conflicts early, before they start festering and turn into full-fledged disputes. When potential conflicts are detected, the board proposes solutions, which, given the expertise and prestige of its members, are likely to be accepted by the parties. Referral of a dispute triggers an evaluation by the board, which is done in an informal manner, typically by discussion with the parties during a regular site visit. The board controls the discussion, but each party is given a full opportunity to state its views, and the dispute review board is free to ask questions and to request documents and other evidence. The advantages of conducting hearings at the job site, soon after the events have occurred and before adversarial positions have hardened, are obvious. The board then meets privately and seeks to formulate a recommendation or a decision. If the parties do not accept these proposals and disputes do arise, the board, if authorized to do so by the parties, is in a unique position to solve them expeditiously because of its familiarity with the problems and contractual documents.

26. Given their usually long duration, many circumstances relevant to the execution of privately financed infrastructure projects may change before the end of the concession term. While the impact of some changes may be automatically covered in the project agreement (see chap. IV, "Construction and operation of infrastructure", paras. 126-130) there are changes that might not lend themselves easily to inclusion in an automatic adjustment mechanism or that the parties may prefer to exclude from such a mechanism. It is therefore important for the parties to establish mechanisms for dealing with disputes that may arise in connection with changing circumstances. This is of particular significance for the operational phase of the project. Where the parties have agreed on rules that allow a revision of the terms of the project agreement following certain circumstances, the question may arise as to whether those circumstances have occurred and, if so, how the contractual terms should be changed or supplemented. With a view to facilitating a resolution of possible disputes and avoiding a stalemate in case the parties are unable to agree on a contract revision, it is advisable for the parties to clarify whether and to what extent certain contractual terms may be changed or supplemented by the dispute review board. It may be noted, in this context, that the parties might not always be able to rely on an arbitral tribunal or a domestic court for that purpose. Indeed, under some legal systems, courts and arbitrators are not competent to change or supplement contractual terms. Under other legal systems, courts and arbitrators may do so only if they are expressly so authorized by the parties. Under yet other legal systems, arbitrators may do so but courts may not.

27. The law governing arbitral or judicial proceedings may determine the extent to which the parties may authorize arbitrators or a court to review a decision of the dispute review board. Excluding such review has the advantage that the decision of the dispute review board would be immediately final and binding. However, permitting such a review gives the parties greater assurance that the decision will be correct. Early clauses on dispute review boards did not

provide that their recommendations would become binding if not challenged in arbitral or judicial proceedings. In practice, however, the combination of the persuasive force of unanimous recommendations by independent experts agreed by the parties has led both contracting authorities and project companies to accept the recommendations voluntarily rather than litigate. Recent contract provisions on dispute review boards usually provide that a decision of the board, while not immediately binding on the parties, becomes binding unless one or both parties refer the dispute to arbitration or initiate judicial proceedings within a specified period of time. Apart from avoiding potentially protracted litigation, the parties often take into account the potential difficulty of overcoming what might be regarded by the court or arbitral tribunal as a powerful recommendation, inasmuch as it had been made by independent experts familiar with the project from the outset and was based on contemporaneous observation of the project prior to, and at the time of, the dispute having first arisen.

28. Although this occurs very rarely, the parties may agree to make the board's decision final and binding. It should be noted, however, that despite the parties' agreement to be bound by the board's decision, under many legal systems, the decision by the dispute review board, while binding as a contract, may not be enforceable in a summary proceeding, such as a proceeding for the enforcement of an arbitral award, since it does not have the status of an arbitral award. If the parties contemplate providing for proceedings before a dispute review board, it will be necessary for them to settle various aspects of those proceedings in the project agreement. It would be desirable for the project agreement to delimit as precisely as possible the authority conferred upon the dispute review board. With regard to the nature of their functions, the project agreement might authorize the dispute review board to make findings of fact and to order interim measures. It may specify the functions to be performed by the dispute review board and the type of issues with which they may deal. If the parties are permitted to initiate arbitral or judicial proceedings within a specified period of time after the decision is rendered, the parties might specify that findings of fact made by a dispute review board are to be regarded as conclusive in arbitral or judicial proceedings. The project agreement might also obligate the parties to implement a decision by the dispute review board concerning interim measures or a decision on the substance of specified issues; if the parties fail to do so, they will be considered as having failed to perform a contractual obligation. Regarding the duration of the board's functions, the project agreement may provide that the board will continue to function for a certain period beyond the expiry or termination of the project agreement, in order to deal with disputes that may arise at that stage (for example, disputes as to the condition of and compensation due for assets handed over to the contracting authority).

(j) Non-binding arbitration

29. This procedure is sometimes used when less adversarial methods such as facilitated negotiation, conciliation or dispute review board procedures have been unsuccessful. Non-binding arbitration is conducted in the same manner as binding arbitration, and the same rules may be used except that the procedure ends with a recommendation. The procedure contemplates that the parties will proceed directly to litigation if the dispute is still unresolved under non-binding arbitration. Those who choose this procedure do so (a) if they have reservations about the binding nature of arbitration; or (b) as an incentive to avoid both arbitration and litigation, arbitration because it would seem redundant to go through the same procedure twice and litigation because of its length and cost.

(k) Arbitration

30. In recent years, arbitration has been used increasingly for settling disputes arising under privately financed infrastructure projects. Arbitration is typically used both for the settlement of disputes that arise during the construction or operation of the infrastructure facility and for the settlement of disputes related to the expiry or termination of the project agreement. Arbitration is preferred by private investors and lenders, in particular foreign ones, since arbitral proceedings may be structured by the parties so as to be less formal than judicial proceedings and better suited to the needs of the parties and to the specific features of the disputes likely to arise under the project agreement. The parties can choose as arbitrators persons who have expert knowledge of the particular type of project. They may choose the place where the arbitral proceedings are to be conducted. They can also choose the language or languages to be used in the arbitral proceedings. Arbitral proceedings may be less disruptive of business relations between the parties than judicial proceedings. The proceedings and arbitral awards can be kept confidential, while judicial proceedings and decisions usually cannot. Furthermore, the enforcement of arbitral awards in countries other than the country in which the award was rendered is facilitated by the wide acceptance of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958.[2]

31. With regard, in particular, to infrastructure projects involving foreign investors, it may be noted that a framework for the settlement of disputes between the contracting authority and foreign companies participating in a project consortium may be provided through adherence to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States.[3] The Convention, which has thus far been adhered to by 131 States, established the International Centre for the Settlement of Investment Disputes (ICSID). ICSID is an autonomous international organization with close links to the World Bank. ICSID provides facilities for the conciliation and arbitration of disputes between member countries and investors who qualify as nationals of other member countries. Recourse to ICSID conciliation and arbitration is voluntary. However, once the parties to a contract or dispute have consented to arbitration under the ICSID Convention, neither can withdraw its consent unilaterally. All ICSID members, whether or not parties to the dispute, are required by the Convention to recognize and enforce ICSID arbitral awards. The consent of the parties to ICSID arbitration may be given with regard to an existing dispute or with respect to a defined class of future disputes. The consent of the parties need not, however, be expressed in relation to a specific project; a host country might in its legislation on the promotion of investment offer to submit disputes arising out of certain classes of investment to the jurisdiction of ICSID and the investor might give its consent by accepting the offer in writing.

32. Bilateral investment agreements may also provide a framework for the settlement of disputes between the contracting authority and foreign companies. In these treaties, the host State typically extends to investors that qualify as nationals of the other signatory State a number of assurances and guarantees (see chap. VII, "Other relevant areas of law", paras. 4-6) and expresses its consent to arbitration, for instance, by referral to ICSID or to an arbitral tribunal applying the UNCITRAL Arbitration Rules.

(i) Sovereign immunity

33. When arbitration is allowed and agreed upon between the parties to the project agreement, the implementation of an agreement to arbitrate may be frustrated or hindered if the contracting authority is able to plead sovereign immunity, either as a bar to the commencement of arbitral proceedings or as a defence against recognition and enforcement of the award. Sometimes the law on this matter is not clear, which may raise concerns with the interested parties (for instance, the concessionaire, project promoters and lenders) that an agreement to

arbitrate might not be effective. In order to address such possible concerns, it is advisable to review the law on this topic and to indicate the extent to which the contracting authority may raise a plea of sovereign immunity.

34. In addition, a contracting authority against which an award has been issued may raise a plea of immunity from execution against public property. There is a diversity of approaches to the question of sovereign immunity from execution. For example, under some national laws immunity does not cover governmental entities when engaged in commercial activities. In other national laws a link is required between the property to be attached and the claim in that, for example, immunity cannot be pleaded in respect of funds allocated for economic or commercial activity governed by private law upon which the claim is based or that immunity cannot be pleaded with respect to assets set aside by the State to pursue its commercial activities. In some countries, it is considered that it is for the Government to prove that the assets to be attached are in non-commercial use.

35. In some contracts involving entities that might plea sovereign immunity, clauses have been included to the effect that the Government waives its right to plead sovereign immunity. Such a consent or waiver might be contained in the project agreement or an international agreement; it may be limited to recognizing that certain property is used or intended to be used for commercial purposes. Such written clauses may be necessary inasmuch as it is not clear whether the conclusion of an arbitration agreement and participation in arbitral proceedings by the governmental entity constitutes an implied waiver of sovereign immunity from execution.

36. The legislator may wish to review its laws on this matter and, to the extent considered advisable, clarify in which areas contracting authorities may not plead sovereign immunity.

(ii) Effectiveness of the arbitration agreement and enforceability of the award

37. The effectiveness of an agreement to arbitrate depends on the legislative regime where the arbitration takes place. If the legislative regime for arbitration in the host country is seen as unsatisfactory, for instance, because it is found to pose unreasonable restrictions on party autonomy, a party might wish to agree on a place of arbitration outside the host country. It is therefore important for the host country to ensure that the domestic legislative regime for arbitration resolves the principal procedural issues in a manner appropriate for international arbitration cases. Such a regime is contained in the UNCITRAL Model Law on International Commercial Arbitration.[4]

38. If the arbitration takes place outside the host country or if an award rendered in the host country would need to be enforced abroad, the effectiveness of the arbitration agreement would also depend on legislation governing the recognition and enforcement of arbitral awards. The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (see para. 30), inter alia, deals with the recognition of an arbitration agreement and the grounds on which the court may refuse to recognize or enforce an award. The Convention is generally regarded as providing an acceptable and balanced regime for the recognition and enforcement of arbitral awards. The fact that the host country is a party to the Convention is likely to be seen as a crucial element in assessing the legal certainty of binding commitments and of the reliability of arbitration as a method for solving disputes by arbitration with parties from the country. It would also facilitate the enforcement abroad of an arbitral award rendered in the host country.

(l) Judicial proceedings

39. As indicated earlier, in some legal systems, pursuant to mandatory rules of a public law nature, the settlement of disputes arising out of project agreements whereby the concessionaire

is entrusted with the provision of public services is a matter of the exclusive competence of the domestic judiciary or administrative courts. In some countries, governmental agencies lack the power to agree to arbitration, except under specific circumstances (see paras. 7-9), while in other legal systems the parties have the freedom to choose between judicial and arbitral proceedings.

40. Where it is possible for the parties to choose between judicial and arbitral proceedings, the contracting authority may see reasons for leaving any dispute to be resolved by the courts of the host country. Those courts are familiar with the law of the country, which often includes specific legislation directly applicable to the project agreement. Furthermore, the contracting authority and other governmental agencies of the host country that might be involved in the dispute may prefer local courts because of the familiarity with the court procedures and the language of the proceedings. It may also be considered that, to the extent project agreements involve issues of public policy and the protection of public interest, state courts are in a better position to give them proper effect.

41. However, such a view by the contracting authority may not be shared by prospective investors, financiers and other private parties. These parties may consider that arbitration is preferable to judicial proceedings because arbitration, being to a larger degree subject to the agreement of the parties than judicial proceedings, is in a position to resolve a dispute more efficiently. Private investors, in particular foreign ones, may also be reluctant to submit to the jurisdiction of domestic courts functioning under rules unfamiliar to them. In some countries it has been found that allowing the parties to choose the dispute settlement mechanism helped to attract foreign investment for the development of its infrastructure.

42. In considering whether any dispute should be resolved in judicial proceedings or whether an arbitration agreement should be entered into, where such choice is permitted under the applicable law, factors typically taken into account by the parties include, for example, their confidence that the courts competent to decide a dispute will be unbiased and that the dispute will be resolved without inordinate delay. The efficiency of the national judicial system and the availability of forms of judicial relief that are adequate to disputes that might arise under the project agreement are additional factors to be taken into account. Furthermore, in view of the highly technical and complex issues involved in infrastructure projects, the parties will also consider the implications of using arbitrators selected for their particular knowledge and experience as compared to domestic courts which may lack specific knowledge or experience in handling the technical questions in the area where the dispute arose. Another consideration may be the confidentiality of arbitration proceedings, relative informality of arbitral procedures, and the possibly greater flexibility arbitrators may have in awarding appropriate remedies, all of which may be beneficial for preserving and developing the long-term relationship implicit in project agreements.

C. Disputes between the concessionaire and its lenders, contractors and suppliers

43. It is generally accepted in domestic laws that parties to commercial transactions, and in particular international commercial transactions, are free to agree on the forum that will decide in a binding decision any dispute that may arise from those transactions. In international transactions, arbitration has become the preferred method, whether or not it is preceded by, or combined with, conciliation. As to contracts between the concessionaire and the lenders, contractors and suppliers, which invariably form part of privately financed infrastructure projects, in many countries the parties are free to subject disputes to arbitration, to select the

place of arbitration and to determine whether or not any arbitration case should be administered by an arbitral institution. These contracts are generally considered commercial agreements to which, as regards dispute settlement clauses, general rules regarding commercial contracts are applicable. Host countries wishing to establish a hospitable legal climate for privately financed infrastructure projects would be well advised to review their laws with respect to these contracts so as to eliminate any uncertainty regarding the freedom of the parties to agree to dispute settlement mechanisms of their choice.

D. Disputes between the concessionaire and its customers

44. Depending on the type of project, the concessionaire's customers may include various persons and entities, such as, for example, a government-owned utility company that purchases electricity or water from the concessionaire so as to resell it to the ultimate users; commercial companies, such as airlines or shipping lines contracting for the use of the airport or port; or individual persons paying for the use of a toll road. The considerations and policies regarding contracts with the end-purchasers of the goods or services supplied by the project company may vary according to who the parties to those contracts are, the conditions under which the services are provided and the applicable regulatory regime.

45. In some countries, public service providers are required by law to establish special simplified and efficient mechanisms for handling claims brought by their customers. Such special regulation is typically limited to certain industrial sectors and applies to purchases of goods or services by customers. Statutory requirements for the establishment of such dispute settlement mechanisms may apply generally to claims brought by any of the concessionaire's customers or may be limited to customers who are individual persons acting in their non-commercial capacity. The concessionaire's obligation may be limited to the establishment of a mechanism for receiving and dealing with complaints by individual consumers. Such mechanisms may include a special facility or department set up within the project company for receiving and handling claims expeditiously, for instance by making available to the customers standard claim forms or toll-free telephone numbers for voicing grievances. If the matter is not satisfactorily resolved, the customer may have the right to file a complaint with a regulatory agency, if any, which in some countries may have the authority to issue a binding decision on the matter. Such mechanisms are often optional for the consumer and typically do not preclude resort by the aggrieved persons to courts.

46. If the customers are utility companies (such as a power distribution company) or commercial enterprises (for instance, a large factory purchasing power directly from an independent producer) who freely choose the services provided by the concessionaire and negotiate the terms of their contracts, the parties would typically settle any disputes by methods usual in trade contracts, including arbitration. Accordingly, there may not be a need for addressing the settlement of these disputes in legislation relating to privately financed infrastructure projects. However, where the concessionaire's customers are government-owned entities, their ability to agree on dispute settlement methods may be limited by rules of administrative law governing the settlement of disputes involving governmental entities. For countries that wish to allow the use of non-judicial methods, including arbitration, for the settlement of disputes between the concessionaire and its government-owned customers, it is important to remove possible legal obstacles and to provide a clear authorization for those entities to agree on dispute settlement methods (see paras. 7-9).

Notes

[1] For the report of the United Nations Commission on International Trade Law on the work of its thirteenth session, see *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 106 (*Yearbook of the United Nations Commission on International Trade Law*, vol. XI, 1980, part one, chap. II, sect. A (United Nations publication, Sales No. E.81.V.8)). The UNCITRAL Conciliation Rules have also been reproduced in booklet form (United Nations publication, Sales No. E.81.V.6). Accompanying the Rules is a model conciliation clause, which reads: "Where, in the event of a dispute arising out of or relating to this contract, the parties wish to seek an amicable settlement of that dispute by conciliation, the conciliation shall take place in accordance with the UNCITRAL Conciliation Rules as at present in force". The use of the UNCITRAL Conciliation Rules was recommended by the General Assembly in its resolution 35/52 of 4 December 1980.

[2] See United Nations, *Treaty Series*, vol. 330, No. 4739, p. 38, reproduced in the *Register of Conventions and Other Instruments concerning International Trade Law*, vol. II (United Nations publication, Sales No. E.73.V.3).

[3] United Nations *Treaty Series*, vol. ___, No. 8359, p. 160.

[4] For the report of the United Nations Commission on International Trade Law on the work of its eighteenth session, See *Official Records of the General Assembly, Fortieth Session, Supplement No. 17* (A/40/17), para. 332 and annex I. The General Assembly, in its resolution 40/72 of 11 December 1985, recommended that all States give due consideration to the Model Law on International Commercial Arbitration, in view of the desirability of uniformity of the law of arbitral procedures and the specific needs of international commercial arbitration practice.

United Nations A/CN.9/471/Add.8

General Assembly

Distr.: General
10 December 1999

Original: English

United Nations Commission on International Trade Law
Thirty-third session
New York, 12 June-7 July 2000

Privately financed infrastructure projects: draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

VII. Other relevant areas of law

Contents

		Paragraphs	Page
A.	General remarks	1-2	3
B.	Other relevant areas of legislation	3-52	3
1.	Promotion and protection of investment	4-6	3
2.	Property law	7-9	4
3.	Security interests	10-16	4
4.	Intellectual property law	17-21	6
5.	Rules and procedures on compulsory acquisition of private property	22-23	8
6.	Rules on government contracts and administrative law	24-27	8
7.	Private contract law	28-29	9
8.	Company law	30-33	10
9.	Tax law	34-39	11
10.	Accounting rules and practices	40-41	12
11.	Environmental protection	42-44	13

V.99-90758 (E)

		Paragraphs	Page
12.	Consumer protection laws	45-46	14
13.	Insolvency law	47-49	14
14.	Anti-corruption measures	50-52	15
C.	International agreements	53-57	15
1.	Membership in multilateral financial institutions	54	15
2.	General agreements on trade facilitation and promotion	55	16
3.	International agreements on specific industries	56-57	16

A. General remarks

1. The stage of development of the relevant laws of the host country, the stability of its legal system and the adequacy of remedies available to private parties are essential elements of the overall legal framework for privately financed infrastructure projects. By reviewing and, as appropriate, improving its laws in those areas of immediate relevance for privately financed infrastructure projects, the host country will make an important contribution to securing a hospitable climate for private sector investment in infrastructure. Greater legal certainty and a favourable legal framework will translate into a better assessment of country risks by lenders and project sponsors. This will have a positive influence on the cost of mobilizing private capital and reduce the need for governmental support or guarantees (see chap. II, "Project risks and government support", paras. 30-60).

2. Section B points out a few selected aspects of the laws of the host country that, without necessarily dealing directly with privately financed infrastructure projects, may have an impact on their implementation (see paras. 3-52). Section C indicates the possible relevance of a few international agreements for the implementation of privately financed infrastructure projects in the host country (see paras. 53-57).

B. Other relevant areas of law

3. In addition to issues pertaining to legislation directed specifically towards privately financed infrastructure projects, a favourable legal framework also requires supportive provisions in other areas of legislation. Private investment in infrastructure will be encouraged by the existence of legislation that promotes and protects private investment in economic activities. The following paragraphs pinpoint only a few selected aspects of other fields of law that may have an impact on the implementation of infrastructure projects. The existence of adequate legal provisions in those other fields may facilitate a number of transactions necessary to carry out infrastructure projects and help to reduce the perceived legal risk of investment in the host country.

1. Promotion and protection of investment

4. One matter of particular concern for the project consortia and the lenders is the degree of protection afforded to investment in the host country. Foreign investors in the host country will require assurances that they will be protected from nationalization or dispossession without judicial review and appropriate compensation in accordance with the rules in force in the host country and in accordance with international law. Project promoters will also be concerned about their ability, *inter alia*, to bring to the country without unreasonable restriction the qualified personnel required to work with the project, to import needed goods and equipment, to gain access to foreign exchange as needed and to transfer abroad or repatriate their profits or sums needed to repay loans that the company has entered into for the purpose of the infrastructure project. In addition to specific guarantees that may be provided by the Government (see chap. II, "Project risks and government support", paras. 45-50), legislation on promotion and protection of investment may play an important role in connection with privately financed infrastructure projects. For countries that already have adequate investment protection legislation, it may be useful to consider expressly extending the protection provided in such legislation to private investment in infrastructure projects.

5. An increasing number of countries have entered into bilateral investment agreements that aim at facilitating and protecting the flow of investment between the contracting parties. Investment protection agreements usually contain provisions concerning the admission and treatment of foreign investment; transfer of capital between the contracting parties (payment of dividends abroad or repatriation of investment, for example); availability of foreign exchange for transfer or repatriation of proceeds of investment; protection from expropriation and nationalization; and settlement of investment disputes. The existence of such an agreement between the host country and the originating country or countries of the project sponsors may play an important role in their decision to invest in the host country. Depending on its terms, such an agreement may reduce the need for assurances or guarantees by the Government geared to individual infrastructure projects. Multilateral treaties may also be a source of investment protection provisions.

6. Moreover, in a number of countries rules aimed at facilitating and protecting the flow of investment (which also include areas such as immigration legislation, import control and foreign exchange rules) are contained in legislation that might not necessarily be based on a bilateral or multilateral treaty.

2. Property law

7. It is desirable for the property laws of the host country to reflect acceptable international standards, contain adequate provisions on the ownership and use of land and buildings, as well as movable and intangible property, and ensure the concessionaire's ability to purchase, sell, transfer and license the use of property, as appropriate. Constitutional provisions protecting property rights have been found to be important factors in fostering private investment in many countries.

8. Where the concessionaire owns the land on which the facility is built, it is important that the ownership of the land can be clearly and unequivocally established through adequate registration and publicity procedures. The concessionaire and lenders will need clear proof that ownership of the land will not be subject to dispute. They will therefore be reluctant to commit funds to the project if the laws of the host country do not provide adequate means for ascertaining ownership of the land.

9. It is also necessary to provide effective mechanisms for the enforcement of the property and possessory rights granted to the concessionaire against violation by third parties. Enforcement should also extend to easements and rights of way that may be needed by the concessionaire for providing and maintaining the relevant service (such as placing of poles and cables on private property to ensure the distribution of electricity) (see chap. IV, "Construction and operation of infrastructure", paras. 30-35).

3. Security interests

10. As indicated earlier (see chap. IV, "Construction and operation of infrastructure", paras. 52-61), security arrangements in privately financed infrastructure projects may be complex and consist of a variety of forms of security, including fixed security over physical assets of the concessionaire (for example, mortgages or charges), pledges of shares of the concessionaire and assignment of intangible assets (receivables) of the project. While the loan agreements are usually subject to the governing law chosen by the parties, the laws of the host country will in most cases determine the type of security that can be enforced against assets located in the host country and the remedies available.

11. Differences in the type of security or limitations in the remedies available under the laws of the host country may be a cause of concern to potential lenders. It is therefore important to ensure that domestic laws provide adequate legal protection to secured creditors and do not hinder the ability of the parties to establish appropriate security arrangements. Because of the significant differences between legal systems regarding the law of security interests, the *Guide* does not discuss in detail the technicalities of the requisite legislation and the following paragraphs provide only a general outline of the main elements of a modern regime for secured transactions.

12. In some legal systems, security interests can be created in virtually all kinds of assets, including intellectual property, whereas in other systems security interests can only be created in a limited category of assets, such as land and buildings. In some countries, security interests can be created over assets that do not yet exist (future assets) and security may be taken over all of a company's assets, while allowing the company to continue to deal with those assets in the ordinary course of business. Some legal systems provide for a non-possessory security interest, so that security can be taken over assets without taking actual possession of the assets; in other systems, as regards those assets which are not subject to a title registration system, security may only be taken by physical possession or constructive possession. Under some systems, enforcement of the security interest can be undertaken without court involvement, whereas in other systems it may only be enforced through court procedures. Some countries provide enforcement remedies that not only include sale of the asset, but also enable the secured lender to operate the asset either by taking possession or appointing a receiver; in other countries, judicial sale may be the primary enforcement mechanism. Under some systems, certain types of security will rank ahead of preferential creditors, whereas in others the preferential creditors rank ahead of all types of security. In some countries, creation of a security interest is cost-efficient, with minimal fees and duties payable, whereas in other countries it can be costly. In some countries, the value of the amount of security taken may be unlimited, while in others the value of security cannot be excessive in comparison with the debt owed. Some legal systems impose obligations on the secured lender on enforcement of the security, such as the obligation to take steps ensuring that assets will be sold at fair market value.

13. Basic legal protection may include provisions ensuring that fixed security (such as a mortgage) is a registrable interest and that, once such security is registered in the register of title or other public register, any purchaser of the property to which the security attaches should take the property subject to such security. This may be difficult, since in many countries no specialized registers of title exist. Furthermore, security should be enforceable against third parties, which may require that they have the nature of a property right and not a mere obligation, and should entitle the person receiving security to a sale, in enforcement proceedings, of the assets taken as security.

14. Another important aspect concerns the flexibility given to the parties to define the assets that are given as security. In some legal systems, broad freedom is given to the parties in the definition of assets that may be given as security. In some legal systems, it is possible to create security that covers all the assets of an enterprise, making it possible to sell the enterprise as a going concern, which may enable an enterprise in financial difficulties to be rescued while increasing the recovery of the secured creditor. Other legal systems, however, allow only the creation of security that attaches to specific assets and do not recognize security covering the entirety of the debtor's assets. There may also be limitations on the debtor's ability to trade in goods given as security. The existence of limitations and restrictions of this type makes it

difficult or even impossible for the debtor to create security over generically described assets or over assets traded in the ordinary course of its business.

15. Given the long-term nature of privately financed infrastructure projects, the parties may wish to be able to define the assets that are given as security specifically or generally. They may also wish such security to cover present or future assets and assets that might change during the life of the security. It may be desirable to review existing provisions on security interests with a view to including provisions enabling the parties to agree on suitable security arrangements.

16. Thus far, no comprehensive uniform regime or model for the development of domestic security laws has been developed by international intergovernmental bodies. Governments might be advised, however, to take account of various efforts being undertaken in different organizations. A model for the development of modern legislation on security interests is offered in the Model Law on Secured Transactions, which was prepared by the European Bank for Reconstruction and Development (EBRD) to assist legislative reform efforts in central and eastern European countries. Besides general provisions on who can create and who can receive a security right and general rules concerning the secured debts and the charged property, the EBRD Model Law on Secured Transactions covers other matters, such as the creation of security rights, the interests of third parties, enforcement of security and registration proceedings.

[*Note for the Commission: Appropriate reference will be made to the draft convention on assignment in receivables financing developed by the Working Group on International Contract Practices, as well as to other international initiatives (such as the draft model inter-American law on secured transactions currently being considered by the Organization of American States in the context of preparations for the Sixth Inter-American Conference on Private International Law and the UNIDROIT draft convention on international interests in mobile equipment).*]

4. Intellectual property law

17. Privately financed infrastructure projects frequently involve the use of new or advanced technologies protected under patents or similar intellectual property rights. They may also involve the formulation and submission of original or innovative solutions, which may constitute the proponent's proprietary information under copyright protection. Therefore, private investors, national and foreign, bringing new or advanced technology into the host country or developing original solutions will need to be assured that their intellectual property rights will be protected and that they will be able to enforce those rights against infringements, which may require the enactment of criminal law provisions designed to combat infringements of intellectual property rights.

18. A legal framework for the protection of intellectual property may be provided by adherence to international agreements regarding the protection and registration of intellectual property rights. It would be desirable to strengthen the protection of intellectual property rights in line with such instruments as the Paris Convention for the Protection of Industrial Property of 1883.[1] The Convention applies to industrial property in the widest sense, including inventions, marks, industrial designs, utility models, trade names, geographical indications and the repression of unfair competition. The Convention provides that, as regards the protection of industrial property, each contracting State must grant national treatment. It also provides for the right of priority in the case of patents, marks and industrial designs and establishes a few common rules that all the contracting States must follow in relation to patents, marks, industrial

designs, trade names, indications of source, unfair competition and national administrations. A framework for further international patent protection is provided under the Patent Cooperation Treaty of 1970, which makes it possible to seek patent protection for an invention simultaneously in each of a large number of countries by filing an international patent application. In some countries, international standards are supplemented by legislation aimed at affording legal protection to new technological developments, such as legislation that protects intellectual property rights in computer software and computer hardware design.

19. Other important instruments providing international protection of industrial property rights are the Madrid Agreement Concerning the International Registration of Marks of 1891,[2] the Protocol Relating to the Madrid Agreement of 1989 and the Common Regulations under the Madrid Agreement and the Protocol Relating thereto of 1998. The Madrid Agreement provides for the international registration of marks (both trademarks and service marks) at the International Bureau of the World Intellectual Property Organization (WIPO). International registration of marks under the Madrid Agreement has effect in several countries, potentially in all the contracting States (except the country of origin). Furthermore, the Trademark Law Treaty of 1994 simplifies and harmonizes procedures for the application for registration of trademarks, changes after registration and renewal.

20. In the area of industrial designs, the Hague Agreement Concerning the International Deposit of Industrial Designs of 1925[3] provides for the international deposit of industrial designs at the International Bureau of WIPO. The international deposit has, in each of the contracting States designated by the applicant, the same effect as if all the formalities required by the domestic law for the grant of protection had been complied with by the applicant and as if all administrative acts required to that end had been accomplished by the office of that country.

21. The most comprehensive multilateral agreement on intellectual property to date is the Agreement on Trade-Related Aspects of Intellectual Property Rights (the "TRIPS Agreement") which was negotiated under the auspices of the World Trade Organization (WTO) and came into effect on 1 January 1995. The areas of intellectual property that it covers are copyright and related rights (that is, the rights of performers, producers of sound recordings and broadcasting organizations); trademarks, including service marks; geographical indications, including appellations of origin; industrial designs; patents, including the protection of new varieties of plants; the layout-designs of integrated circuits; and undisclosed information, including trade secrets and test data. In respect of each of the main areas of intellectual property covered by it, the TRIPS Agreement sets out the minimum standards of protection to be provided by each contracting party by requiring, first, compliance with the substantive obligations, *inter alia*, of the Paris Convention in its most recent version. The main substantive provisions of the Paris Convention are incorporated by reference and thus become obligations under the TRIPS Agreement. The TRIPS Agreement also adds a substantial number of additional obligations on matters where the pre-existing conventions on intellectual property are silent or were seen as being inadequate. In addition to that, the Agreement lays down certain general principles applicable to all procedures for the enforcement of intellectual property rights. Furthermore, the TRIPS Agreement contains provisions on civil and administrative procedures and remedies, provisional measures, special requirements related to border measures and criminal procedures, which specify, in a certain amount of detail, the procedures and remedies that must be available so that intellectual property rights can effectively be enforced by their holders.

5. Rules and procedures on compulsory acquisition of private property

22. Where the Government assumes responsibility for providing the land required for the implementation of the project, that land may be either purchased from its owners or, if necessary, compulsorily acquired against the payment of adequate compensation by procedures sometimes referred to as "compulsory acquisition" or "expropriation" (see chap. IV, "Construction and operation of infrastructure", paras. 20-22). Many countries have legislation governing compulsory acquisition of private property and that legislation would probably apply to the compulsory acquisition of property required for privately financed infrastructure projects.

23. Compulsory acquisition may be carried out in judicial or administrative proceedings or may be effected by an ad hoc legislative act. In most cases, the proceedings involve both administrative and judicial phases, which may be lengthy and complex. The Government may thus wish to review existing provisions on compulsory acquisition for reasons of public interest with a view to assessing their adequacy to the needs of large infrastructure projects and to determining whether such provisions allow quick and cost-effective procedures, while affording adequate protection to the rights of the owners. To the extent permitted by law, it is important to enable the Government to take possession of the property without unnecessary delay, so as to avoid increased project costs.

6. Rules on government contracts and administrative law

24. In many legal systems belonging to or influenced by the tradition of civil law, the provision of public services may be governed by a body of law known as "administrative law", which regulates a wide range of governmental functions. Such systems operate under the principle that the Government can exercise its powers and functions either by means of an administrative act or an administrative contract. It is also generally understood that, alternatively, the Government may enter into a private contract, subject to the law governing private commercial contracts. The differences between the two types of contract may be significant.

25. Under the concept of the administrative contract, the freedom and autonomy enjoyed by the parties to a private contract are subordinate to the public interest. In some legal systems, the Government has the right to modify the scope and terms of administrative contracts or even terminate them for reasons of public interest, usually subject to compensation for loss sustained by the private contracting party (see chap. V, "Duration, extension and termination of the project agreement", ___). Additional rights might include extensive monitoring and inspection rights, as well as the right to impose sanctions on the private operator for failure to perform. This is often balanced by the requirement that other changes may be made to the contract as may be necessary to restore the original financial equilibrium between the parties and to preserve the contract's general value for the private contracting party (see chap. IV, "Construction and operation of infrastructure", paras. 126-130). In some legal systems, disputes arising out of government contracts are subject to the exclusive jurisdiction of special tribunals dealing solely with administrative matters, which in some countries are separate from the judicial system (see chap. VI, "Settlement of disputes", ___).

26. The existence of a special legal regime applicable to infrastructure operators and public service providers is not limited to the legal systems referred to above. Although in other legal systems influenced by the tradition of common law no such categorical distinction is made between administrative contracts and private contracts, similar consequences may be achieved by different means. While under such systems of law it is frequently held that the rule of law is best maintained by subjecting the Government to ordinary private law, it is generally recognized that the administration cannot by contract fetter the exercise of its sovereign

functions. It cannot hamper its future executive authority in the performance of those governmental functions which affect the public interest. Under the doctrine of sovereign acts, which is upheld in some common law jurisdictions, the Government as contractor is excused from the performance of its contracts if the Government as sovereign enacts laws, regulations or orders in the public interest that prevent that performance. Thus, the law may permit a public authority to interfere with vested contractual rights. Usually such action is limited so that the changes cannot be of such magnitude that the other party could not fairly adapt to them. In those circumstances, the private party is ordinarily entitled to some sort of compensation or equitable adjustment. In anticipation of such possibilities, in some countries a standard "changes" clause is included in a governmental contract that enables the Government to alter the terms on a unilateral basis or that provides for changes as a result of an intervening sovereign act.

27. Special prerogatives for governmental agencies are justified in those legal systems by reasons of public interest. It is however recognized that special governmental prerogatives, in particular the power to alter the terms of contracts unilaterally, may, if improperly used, adversely affect the vested rights of government contractors. For this reason, countries with a well established tradition of private participation in infrastructure projects have developed a series of control mechanisms and remedies to protect government contractors against arbitrary or improper acts by public authorities, such as access to impartial dispute settlement bodies and full compensation schemes for governmental wrongdoing. Where protection of this nature is not afforded, rules of law providing public authorities with special prerogatives may be regarded by potential investors as an imponderable risk, which may discourage them from investing in particular jurisdictions. For this reason, some countries have reviewed their legislation on government contracts so as to provide the degree of protection needed to foster private investment and remove those provisions which gave rise to concern about the long-term contractual stability required for infrastructure projects.

7. Private contract law

28. The laws governing private contracts play an important role in connection with contracts entered into by the concessionaire with subcontractors, suppliers and other private parties. The domestic law on private contracts should provide adequate solutions to the needs of the contracting parties, including flexibility in devising the contracts needed for the construction and operation of the infrastructure facility. Apart from some essential elements of adequate contract law, such as general recognition of party autonomy, judicial enforceability of contract obligations and adequate remedies for breach of contract, the laws of the host country may create a favourable environment for privately financed infrastructure projects by facilitating contractual arrangements likely to be used in those projects. An adequate set of rules of private international law is also important, given the likelihood that contracts entered into by the concessionaire will include some international elements.

29. Where new infrastructure is to be built, the concessionaire may need to import large quantities of supplies and equipment. Greater legal certainty for such transactions will be ensured if the laws of the host country contain provisions specially adapted to international sales contracts. A particularly suitable legal framework may be provided by adherence to the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980)[4] or other international instruments dealing with specific contracts, such as the UNIDROIT Convention on International Financial Leasing (Ottawa, 1988),[5] drawn up by the International Institute for the Unification of Private Law (UNIDROIT).

8. Company law

30. In most projects involving the development of a new infrastructure, the project promoters will establish the project company as a separate legal entity in the host country (see chap. IV, "Construction and operation of infrastructure", paras. 12-18). It is recognized that the project company may take various forms in different countries, which may not necessarily entail a corporation. As in most cases it is a corporate form that is selected, it is particularly important for the host country to have adequate company laws with modern provisions on essential matters such as establishment procedures, corporate governance, issuance of shares and their sale or transfer, accounting and financial statements and protection of minority shareholders. Furthermore, the recognition of the investors' ability to establish separate entities to serve as special-purpose vehicles for raising financing and disbursing funds may facilitate the closing of project finance transactions (see chap. IV, "Construction and operation of infrastructure", para. 59).

31. Although various corporate forms may be used, a common characteristic is that the concessionaire's owners (or shareholders) will require that their liability be limited to the value of their shares in the company's capital. If it is intended that the concessionaire will offer shares to the public, limited liability will be necessary, as the prospective investors will usually only purchase those shares for their investment value and will not be closely involved in the operation of the concessionaire. It is therefore important that the laws of the host country provide adequately for the limitation of liability of shareholders. Furthermore, adequate provisions governing the issuance of bonds, debentures or other securities by commercial companies will enable the concessionaire to obtain funds from investors on the security market, thus facilitating the financing of certain infrastructure projects.

32. Legislation should establish the responsibilities of directors and administrators of the concessionaire, including the basis for criminal responsibility. It can also set out provisions for the protection of third parties affected by any breach of corporate responsibility. Modern company laws often contain specific provisions regulating the conduct of managers so as to prevent conflicts of interest. Provisions of this type require that managers act in good faith in the best interest of the company and do not use their position to foster their own or any other person's financial interests to the detriment of the company. Provisions intended to curb conflicts of interest in corporate management may be particularly relevant in connection with infrastructure projects, where the concessionaire may wish to engage its own shareholders, at some stage of the project, to perform work or provide services in connection with it (see chap. IV, "Construction and operation of infrastructure", paras. 100 and 101).

33. It is important for the law to regulate adequately the decision-making process both for meetings of the shareholders and meetings of management organs of the company (the board of directors or supervisory board, for example). Protection of shareholders' rights and, in particular, protection for minority shareholders from abuse by controlling or majority shareholders are important elements of modern company laws. Mechanisms for the settlement of disputes among shareholders are also critical. It is useful to recognize the right of the shareholders to regulate a number of additional matters concerning the management of the concessionaire through agreements among themselves or through management contracts with the directors of the concessionaire.

9. Tax law

34. In addition to possible tax incentives that may be generally available in the host country or that may be specially granted to privately financed infrastructure projects (see chap. II, "Project risks and government support", paras. 51-54), the general taxation regime of the host country plays a significant role in the investment decisions of private companies. Beyond an assessment of the impact of taxation in the project cost and the expected margin of profit, private investors consider questions such as the overall transparency of the domestic taxation system, the degree of discretion exercised by taxation authorities, the clarity of guidelines and instructions issued to taxpayers and the objectivity of criteria used to calculate tax liabilities. This may be a complex matter, in particular in those countries where the authority to establish or increase taxes or to enforce tax legislation has been decentralized.

35. Privately financed infrastructure projects are typically highly leveraged and require a predictable cash flow. For that reason, it is crucial for all potential tax implications to be readily assessable throughout the life of the project. Unanticipated changes in the taxes that reduce that cash flow can have serious consequences for the project. In some countries, the Government is authorized to enter into agreements with the investors for the purpose of guaranteeing that the cash flow of the project will not be adversely affected by unexpected increases in taxation. Such arrangements are sometimes referred to as "tax stabilization agreements". However, the Government may be restrained, by constitutional law or for political reasons, from providing this type of guarantee, in which case the parties may agree on compensation or contractual revision mechanisms for dealing with cost increases due to tax changes (see also chap. IV, "Construction and operation of infrastructure", paras. 122-125).

36. Most national tax regimes fall into one of three general categories. One approach is worldwide taxation with credits, in which all income earned anywhere is taxed in the home country and double taxation is avoided through the use of a foreign tax credit system; home country taxes are reduced by the amount of foreign taxes already paid. If this approach is used by an investor's home country, the investor's tax liability can be no less than it would be at home. Under a different taxation approach, the foreign income that has already been subject to foreign tax is exempt from taxation by the home country of the investor. Under a territorial approach, foreign income is exempt from home country taxation altogether. Investors in home countries that use the latter two systems of taxation would benefit from tax holidays and lower tax rates in the host country, but such tax relief would offer no incentive to an investor located in a tax haven.

37. The parties involved in the project may have different concerns over potential tax liability. Investors are usually concerned about the taxation of profits earned in the host country, taxation on payments made to contractors, suppliers, investors and lenders, and tax treatment of any capital gains (or losses) when the concessionaire is wound up. Investors may find that payments used to reduce taxes under their home country regime (such as payments for interest on borrowed funds, investigation costs, bidding costs and foreign exchange losses) may not be available in the host country, or vice versa. Since foreign tax credits are only allowed for foreign income taxes, investors need to ensure that any income tax paid in the host country satisfies the definition of income tax of their own country's taxing authority. Similarly, the project company in the host country may be treated for tax purposes as a different type of entity in the home country. In projects where the assets become public property, this may preclude deductions for depreciation under the laws of the home country.

38. One particular problem of privately financed infrastructure projects involving foreign investment is the possibility that foreign companies participating in a project consortium may be exposed to double taxation, that is, taxation of profits, royalties and interests in their own

home countries as well as in the host country. The timing of tax payments and requirements to pay withholding taxes can also pose problems. A number of countries have entered into bilateral agreements to eliminate or at least reduce the negative effects of double taxation and the existence of such agreements between the host country and the home countries of the project sponsors often plays a role in their tax considerations.

39. Ultimately, it is the cumulative effect of all taxes combined that needs to be taken into consideration. For example, there may be taxes imposed by more than one level of taxing authority; in addition to taxation by the national Government, the concessionaire may also face municipal or provincial taxes. There may also be certain levies other than income taxes, which often are due and payable before the concessionaire has earned any revenues. These include sales taxes, sometimes referred to as "turnover taxes", value-added taxes, property taxes, stamp duties and import duties. Sometimes special provisions can be made to offer relief from these payments as well.

10. Accounting rules and practices

40. In several countries, companies are required by law to follow internationally acceptable standard accounting practices and retain the services of professional accountants or accounting auditors. Among the reasons for this is that the adoption of standard accounting practices is a measure taken to achieve uniformity in the valuation of businesses. In connection with the selection of the concessionaire, the use of standard accounting practices may also facilitate the task of evaluating the financial standing of bidders in order to determine whether they meet the pre-selection criteria required by the contracting authority (see chap. III, "Selection of the concessionaire", paras. 38-40). Standard accounting practices are also essential for carrying out audits of the profits of companies, which may be required for the application of tariff structures and the monitoring of the concessionaire's performance by the regulatory body (see chap. IV, "Construction and operation of infrastructure", paras. 39-46).

41. Special accounting rules for infrastructure operators have also been introduced in some countries to take into account the particular revenue profile of infrastructure projects. Projects involving the construction of infrastructure facilities, in particular roads and other transportation facilities, are typically characterized by a relatively short investment period, with high financial cost and no revenue stream, followed by a longer period with increasing revenue and decreasing financial cost and, under normal circumstances, stable operating costs. Accordingly, if traditional accounting rules were applied, the particular financial structure of such projects would need to be recorded in the project company's accounts as a period of continuous negative results followed by a long period of net profit. This would not only have negative consequences, for instance, for the project company's credit rating during the construction phase, but might also result in a disproportionate tax debt during the operational phase of the project. In order to avoid such a distortion, some countries have adopted special accounting rules for companies undertaking infrastructure projects that take into account the fact that the financial results of privately financed infrastructure projects may only become positive on a medium-term basis. Those special rules typically authorize infrastructure developers to defer part of the financial cost accrued during the deficit phase to the subsequent financial years, in accordance with financial schedules provided in the project agreement. However, the special accounting rules are typically without prejudice to other rules of law that may prohibit the distribution of dividends during financial years closed with negative results.

11. Environmental protection

42. Environmental protection encompasses a wide variety of issues, ranging from handling of wastes and hazardous substances to relocation of persons displaced by large land-use projects. It is widely recognized that environmental protection is a critical prerequisite to sustainable development. Environmental protection legislation is likely to have a direct impact on the implementation of infrastructure projects at various levels, and environmental matters are among the most frequent causes of disputes. Environmental protection laws may include various requirements, such as the consent by various environmental authorities, evidence of no outstanding environmental liability, assurances that environmental standards will be maintained,commitments to remedy environmental damage and notification requirements. These laws often require prior authorization for the exercise of a number of business activities, which may be particularly stringent for some types of infrastructure (for instance, waste water treatment, waste collection, the coal-fired power sector, power transmission, roads and railways).

43. It is therefore advisable to include in legislation measures that make obligations arising from environmental laws transparent. It is important to ensure the highest possible degree of clarity in provisions concerning the tests that may be applied by the environmental authorities, the documentary and other requirements to be met by the applicants, the conditions under which licences are to be issued and the circumstances that justify the denial or withdrawal of a licence. Particularly important are provisions that guarantee the applicant's access to expeditious appeals procedures and judicial recourse, as appropriate. It may also be advisable to ascertain to the extent possible, prior to the final award of the project, whether the conditions for obtaining the required environmental licences are met. In some countries, special public authorities or advocacy groups may have the right to institute legal proceedings to seek to prevent environmental damage, which may include the right to seek the withdrawal of a licence deemed to be inconsistent with applicable environmental standards. In some of those countries, it has been found useful to involve representatives of the public in the proceedings that lead to the issuance of environmental licences. The legislation may also establish the range of penalties that may be imposed and specify the parties that may be held responsible for the damage.

44. Adhering to treaties relating to the protection of the environment may help to strengthen the international regime of environmental protection. A large number of international instruments have been developed in the past decades to establish common international standards. These include the following: Agenda 21[6] and the Rio Declaration on Environment and Development,[7] adopted by the United Nations Conference on Environment and Development in 1992; the World Charter for Nature (General Assembly resolution 37/7, annex); the Basel Convention on the Control of Transboundary Movement of Hazardous Wastes and Their Disposal of 1989; the Convention on Environmental Impact Assessment in a Transboundary Context of 1991; and the Convention on the Protection and Use of Transboundary Watercourses and International Lakes of 1992.

12. Consumer protection laws

45. A number of countries have special rules of law on consumer protection. Consumer protection laws vary greatly from country to country, both in the way they are organized and in their substance. Nevertheless, consumer protection laws often include provisions such as favourable time limits for asserting claims and enforcing contractual rights; special rules for the interpretation of contracts whose terms are not usually negotiated with the consumer (sometimes referred to as "adhesion contracts"); extended warranties in favour of consumers;

special termination rights; access to simplified dispute settlement instances (see also chap. VI, "Settlement of disputes", ___) or other protective measures.

46. From the concessionaire's perspective, it is important to consider whether the host country's laws on consumer protection may limit or hinder the concessionaire's ability to enforce, for instance, its right to obtain payment for the services provided, to adjust prices or to discontinue services to customers who breach essential terms of their contracts or violate essential conditions for the provision of the services.

13. Insolvency law

47. The insolvency of an infrastructure operator or public service provider raises a number of issues that have led some countries to establish special rules to deal with such situations, including rules that enable the contracting authority to take the measures required to ensure the continuity of the project (see chap. V, "Duration, extension and termination of the project agreement", ___). The continuity in the provision of the service may be achieved by means of a legal framework that allows for the rescue of enterprises facing financial difficulties, such as reorganization and similar proceedings. In the event that bankruptcy proceedings become inevitable, the secured lenders will be specially concerned about provisions concerning secured claims, in particular as to whether secured creditors may foreclose on the security despite the opening of bankruptcy proceedings, whether secured creditors are given priority for payments made with the proceeds of the security and how claims of secured creditors are ranked. As noted earlier, a substantial portion of the concessionaire's debt takes the form of "senior" loans, with the lenders requiring precedence of payment over payment of the subordinated debt of the concessionaire (see "Introduction and background information on privately financed infrastructure projects", para. 58). The extent to which the lenders will be able to enforce such subordination arrangements will depend on the rules and provisions of the laws of the country that govern the ranking of creditors in insolvency proceedings. The legal recognition of party autonomy on the establishment of contractual subordination of different classes of loans may facilitate the financing of infrastructure projects.

48. Among the issues that the legislation should address are the following: the question of the ranking of creditors; the relationship between the insolvency administrator and creditors; legal mechanisms for reorganization of the insolvent debtor; special rules designed to ensure the continuity of the public service in case of insolvency of the concessionaire; and provisions on avoidance of transactions entered into by the debtor shortly before the opening of the insolvency proceedings.

49. In large infrastructure projects, the insolvency of the project company is likely to involve creditors from more than one country or affect assets located in more than one country. It may therefore be desirable for the host country to have provisions in place that facilitate judicial cooperation, court access for foreign insolvency administrators and recognition of foreign insolvency proceedings. A suitable model that may be used by countries wishing to adopt legislation for that purpose is provided in the UNCITRAL Model Law on Cross-Border Insolvency.

14. Anti-corruption measures

50. The investment and business environment in the host country may also be enhanced by measures to fight corruption in the administration of government contracts. It is particularly important for the host country to take effective and concrete action to combat bribery and

related illicit practices, in particular to pursue effective enforcement of existing laws prohibiting bribery.

51. The enactment of laws that incorporate international agreements and standards on integrity in the conduct of public business may represent a significant step in that direction. Important standards are contained in two resolutions of the United Nations General Assembly: resolution 51/59 of 12 December 1996, by which the Assembly adopted the International Code of Conduct for Public Officials, and resolution 51/191 of 16 December 1996, by which it adopted the United Nations Declaration against Corruption and Bribery in International Commercial Transactions. Other important instruments include the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions of 1997, which was negotiated under the auspices of the Organisation for Economic Cooperation and Development.

52. Furthermore, it is important that the rules covering the functioning of contracting authorities and the monitoring of public contracts ensure the required degree of transparency and integrity. Where such rules do not exist, appropriate legislation and regulations should be developed and adopted. Simplicity and consistency, coupled with the elimination of unnecessary procedures that prolong the administrative procedures or make them cumbersome, are additional elements to be taken into consideration in this context.

C. International agreements

53. In addition to the internal legislation of the host country, privately financed infrastructure projects may be affected by international agreements entered into by the host country. The implications of certain international agreements is discussed briefly below, in addition to other international agreements mentioned throughout the legislative guide.

1. Membership in multilateral financial institutions

54. Membership in multilateral financial institutions such as the World Bank, the International Development Association, the International Finance Corporation, the Multilateral Investment Guarantee Agency and the regional development banks may have a direct impact on privately financed infrastructure projects in various ways. Firstly, the host country's membership in those institutions is typically a requirement in order for projects in the host country to receive financing and guarantees provided by those institutions. Secondly, the rules on financing and guarantee instruments provided by those institutions typically contain a variety of terms and conditions of direct relevance for the terms of the project agreement and the loan agreements negotiated by the concessionaire (for example, a clause of negative pledge of public assets and provision of counter-guarantees in favour of the multilateral financial institution). Lastly, multilateral financial institutions usually follow a number of policy objectives whose implementation they seek to ensure in connection with projects supported by them (such as adherence to internationally acceptable environmental standards, long-term sustainability of the project beyond the initial concession period and transparency and integrity in the selection of the concessionaire and the disbursement of their loans).

2. General agreements on trade facilitation and promotion

55. A number of multilateral agreements have been negotiated to promote free trade at the global level. The most notable of those agreements have been negotiated under the auspices of the General Agreement on Tariffs and Trade and later WTO. Those agreements may contain general provisions on trade promotion and facilitation of trade in goods (such as a most-

favoured-nation clause or prohibition of the use of quantitative restrictions and other discriminatory trade barriers) and on the promotion of fair trade practices (such as prohibition of dumping and limitations on the use of subsidies). Some specific agreements are aimed at the removal of barriers for the provision of services by foreigners in the contracting States or promoting transparency and eliminating discrimination of suppliers in public procurement. Those agreements may be relevant for national legislation on privately financed infrastructure projects that contemplates restrictions on the participation of foreign companies in infrastructure projects or establishes preferences for national entities or for the procurement of supplies on the local market.

3. International agreements on specific industries

56. In the context of the negotiations on basic telecommunications concluded as part of the General Agreement on Trade in Services (GATS), a number of States members of WTO representing most of the world market for telecommunication services have made specific commitments to facilitate trade in telecommunication services. It should be noted that all WTO member States (even those which have not made specific telecommunication commitments) are bound by the general GATS rules on services, including specific requirements dealing with most-favoured-nation treatment, transparency, regulation, monopolies and business practices. The WTO telecommunication agreement adds sector- and country-specific commitments to the overall GATS agreement. Typical commitments cover the opening of various segments of the market, including voice telephony, data transmission and enhanced services, to competition and foreign investment. Legislators of current or prospective WTO member States should thus ensure that the country's telecommunication laws are consistent with the GATS agreement and their specific telecommunication commitments.

57. Another important sector-specific agreement at the international level is the Energy Charter Treaty, concluded at Lisbon on 17 December 1994 and in force since 16 April 1998, which has been enacted to promote long-term cooperation in the energy field. The Treaty provides for various commercial measures, such as the development of open and competitive markets for energy materials and products and the facilitation of transit and access to and transfer of energy technology. Furthermore, the Treaty aims at avoiding market distortions and barriers to economic activity in the energy sector and promotes the opening of capital markets to encourage the flow of capital in order to finance trade in materials and products. The Treaty also contains regulations about investment promotion and protection: equitable conditions for investors, monetary transfers related to investments, compensation for losses due to war, civil disturbance or other similar events and compensation for expropriation.

Notes

[1] As revised at Brussels on 14 December 1900, at Washington, D.C., on 2 June 1911, at The Hague on 6 November 1925, at London on 2 June 1934, at Lisbon on 31 October 1958 and at Stockholm on 14 July 1967 and as amended on 2 October 1979.

[2] As revised at Brussels on 14 December 1900, at Washington, D.C., on 2 June 1911, at The Hague on 6 November 1925, at London on 2 June 1934, at Nice on 15 June 1957 and at Stockholm on 14 July 1967.

[3] With the Additional Act of Monaco of 1961, the Complementary Act of Stockholm of 1967 as amended on 28 September 1979 and the Regulations Under the Hague Agreement Concerning the International Deposit of Industrial Designs of 1998.

[4] *Official Records of the United Nations Conference on Contracts for the International Sale of Goods, Vienna, 10 March-1 April 1980* (United Nations publication, Sales No. E.82.V.5), part I.

[5] *Acts and Proceedings of the Diplomatic Conference for the adoption of the draft Unidroit Conventions on International Factoring and International Financial Leasing, Ottawa, 9-28 May 1988*, vol. I.

[6] Report of the United Nations Conference on Environment and Development, Rio de Janeiro, 3-14 June 1992 (United Nations publication, Sales No. E.93.I.8 and corrigenda), vol. I: *Resolutions Adopted by the Conference*, resolution 1, annex II.

[7] Ibid., annex I.

UNITED NATIONS **A**

General Assembly

Distr.
GENERAL

A/CN.9/471/Add.9
2 December 1999

ORIGINAL: ENGLISH

UNITED NATIONS COMMISSION
ON INTERNATIONAL TRADE LAW
Thirty-third session
New York, 12 June - 7 July 2000

PRIVATELY FINANCED INFRASTRUCTURE PROJECTS

Draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

CONSOLIDATED LEGISLATIVE RECOMMENDATIONS

CONTENTS

	Recommendations	*Page*
I. General legislative and institutional framework	1-11	4
Constitutional and legislative framework	1	4
Scope of authority to award concessions	2-5	4
Administrative coordination	6	4
Authority to regulate infrastructure services	7-11	4
II. Project risks and government support	12-13	5
Project risks and risk allocation	12	5
Government support	13	5
III. Selection of the concessionaire	14-38	5
General considerations	14	5
Preselection of bidders	15-17	5
Procedure for requesting proposals	18-27	6
Direct negotiations	28-29	8

Unsolicited proposals	30-35	9
Review procedures	36	10
	Recommendations	*Page*
Notice of project award	37	10
Record of selection and award proceedings	38	10
IV. Construction and operation of infrastructure	39-59	10
General provisions on the project agreement	39-40	10
Organization of the concessionaire	41-42	10
The project site and easements	43-44	10
Financial arrangements	45-47	11
Security interests	48	11
Assignment of the concession	49	11
Transfer of controlling interest in the project company	50	11
Construction works	51	11
Infrastructure operation	52-54	12
General contractual arrangements	55-59	12
V. Duration, extension and termination of the project agreement	60-67	13
Duration and extension of the project agreement	60-61	13
Termination of the project agreement	62-64	13
Consequences of expiry or termination of the project agreement	65-67	14
VI. Settlement of disputes	68-70	15
Disputes between the contracting authority and the concessionaire	68-68 *bis*	15
Disputes between the concessionaire and its lenders, contractors and suppliers	69	15
Disputes between the concessionaire and its customers	70	15

FOREWORD

Each chapter of the Guide contains a set of recommended legislative principles entitled "Legislative Recommendations". The Legislative Recommendations are intended to assist in the establishment of a legislative framework favourable to privately financed infrastructure projects. The Legislative Recommendations contained in the Guide are followed by notes which offer an analytical introduction with references to financial, regulatory, legal, policy, and other issues raised in the subject area. The full text of all Legislative Recommendations contained in the Guide is reproduced hereafter for ease of reference. The user is advised to read the Legislative Recommendations together with the notes, which provide background information to enhance the understanding of the Legislative Recommendations.

The Legislative Recommendations deal with matters which it is important to address in legislation specifically concerned with privately financed infrastructure projects. They do not deal with other areas of law which, as discussed in notes to the Legislative Recommendations, also have an impact on privately financed infrastructure projects. Moreover, the successful implementation of privately financed infrastructure projects typically requires various measures beyond the establishment of an appropriate legislative framework, such as adequate administrative structures and practices, organizational capability, technical expertise, appropriate human and financial resources, economic stability.

For host countries wishing to promote privately financed infrastructure projects it is recommended that the following principles should be implemented by the law:

I. GENERAL LEGISLATIVE AND INSTITUTIONAL FRAMEWORK

Constitutional and legislative framework (see chap. I, "General legislative and institutional framework", paras. 2-14)

Recommendation 1. The legislative and institutional framework for the implementation of privately financed infrastructure projects should ensure transparency, fairness, and the long-term sustainability of projects. Undesirable restrictions to private sector participation in infrastructure development and operation should be eliminated.

Scope of authority to award concessions (see chap. I, "General legislative and institutional framework", paras. 15-22)

Recommendation 2. The law should identify the public authorities of the host country (including, as appropriate, national, provincial and local authorities) which are empowered to enter into agreements for the implementation of privately financed infrastructure projects.

Recommendation 3. Privately financed infrastructure projects may include concessions for the construction and operation of new infrastructure facilities and systems or the maintenance, modernization, expansion and operation of existing infrastructure facilities and systems.

Recommendation 4. The law should identify the sectors or types of infrastructure in respect of which concessions may be granted.

Recommendation 5. The law should specify the extent to which a concession might extend to the entire region under the jurisdiction of the respective contracting authority, to a geographical subdivision thereof or to a discrete project, and whether it might be awarded with or without exclusivity, as appropriate, in accordance with rules and principles of law, statutory provisions, regulations and policies applying to the sector concerned. Contracting authorities might be jointly empowered to award concessions beyond a single jurisdiction.

Administrative coordination (see chap. I, "General legislative and institutional framework", paras. 23-29)

Recommendation 6. Institutional mechanisms should be established to coordinate the activities of the public authorities responsible for issuing approvals, licences, permits or authorizations required for the implementation of privately financed infrastructure projects in accordance with statutory or regulatory provisions on the construction and operation of infrastructure facilities of the type concerned.

Authority to regulate infrastructure services (see chap. I, "General legislative and institutional framework", paras. 30-53)

Recommendation 7. The authority to regulate infrastructure services should not be entrusted to entities which directly or indirectly provide infrastructure services.

Recommendation 8. Regulatory competence should be entrusted to functionally independent bodies with a sufficient level of autonomy to ensure that their decisions are taken without political interference or inappropriate pressures from infrastructure operators and public service providers.

Recommendation 9. The rules governing regulatory procedures should be published. Regulatory decisions should state the reasons on which they are based and be accessible to interested parties through publication or other means.

Recommendation 10. The law should establish transparent procedures whereby the concessionaire may request a review of regulatory decisions by an independent and impartial body and set forth the grounds on which a request for review may be based and the availability of court review.

Recommendation 11. Where appropriate, special procedures should be established for handling disputes among public service providers concerning alleged violations of laws and regulations governing the relevant sector.

II. PROJECT RISKS AND GOVERNMENT SUPPORT

Project risks and risk allocation (see chap. II, "Project risks and Government support", paras. 8-29)

Recommendation 12. No unnecessary statutory or regulatory limitations should be placed upon the contracting authority's ability to agree on an allocation of risks that is suited to the needs of the project.

Government support (see chap. II, "Project risks and government support", paras. 30-60)

Recommendation 13. The law should clearly state which public authorities of the host country may provide financial or economic support to the implementation of privately financed infrastructure projects and which types of support they are authorized to provide.

III. SELECTION OF THE CONCESSIONAIRE

General considerations (see chap. III, "Selection of the concessionaire", paras. 1-33)

Recommendation 14. The law should provide for the selection of the concessionaire through transparent and efficient competitive procedures adapted to the particular needs of privately financed infrastructure projects.

Preselection of bidders (see chap. III, Selection of the concessionaire", paras. 34-50)

Recommendation 15. The bidders should demonstrate that they meet the preselection criteria which the contracting authority considers appropriate for the particular project, including:

(a) Adequate professional and technical qualifications, human resources, equipment and other physical facilities, as necessary to carry out all the phases of the project, namely engineering, construction, operation and maintenance;

(b) Sufficient ability to manage the financial aspects of the project and capability to sustain the financing requirements for the engineering, construction and operational phases of the project;

(c) Appropriate managerial and organizational capability, reliability and experience, including previous experience in operating public infrastructure.

Recommendation 16. The bidders should be allowed to form consortia to submit proposals, provided that each member of a preselected consortium may participate, either directly or through subsidiary companies, in only one bidding consortium.

Recommendation 17. The contracting authority should elaborate a short list of the preselected bidders which will be subsequently invited to submit proposals upon completion of the preselection phase.

Procedure for requesting proposals (see chap. III, Selection of the concessionaire", paras. 51-84)

Single-stage and two-stage procedure for requesting proposals

Recommendation 18. Upon completion of the preselection proceedings, the contracting authority should invite the preselected bidders to submit final proposals.

Recommendation 19. Notwithstanding the above, the contracting authority may use a two-stage procedure to request proposals from preselected bidders when it is not feasible for the contracting authority to formulate project specifications or performance indicators and contractual terms in a manner sufficiently detailed and precise to permit final proposals to be formulated. Where a two-stage procedure is used, the following provisions apply:

(a) The contracting authority should first call upon the preselected bidders to submit proposals relating to output specifications and other characteristics of the project as well as to the proposed contractual terms;

(b) The contracting authority may convene a meeting of bidders to clarify questions concerning the initial request for proposals;

(c) Following examination of the proposals received, the contracting authority may review and, as appropriate, revise the initial project specifications and contractual terms prior to issuing a final request for proposals.

Content of the final request for proposals

Recommendation 20. The final request for proposals should include at least the following:

(a) General information as may be required by the bidders in order to prepare and submit their proposals;

(b) Project specifications and performance indicators, as appropriate, including the contracting authority's requirements regarding safety and security standards and environmental protection;

(c) The contractual terms proposed by the contracting authority;

(d) The criteria for evaluating the proposals, the relative weight to be accorded to each such criterion and the manner in which they are to be applied in the evaluation of proposals.

Clarifications and modifications

Recommendation 21. The contracting authority may, whether on its own initiative or as a result of a request for clarification by a bidder, modify the final request for proposals by issuing addenda at a reasonable time prior to the deadline for submission of proposals.

Evaluation criteria

Recommendation 22. The criteria for the evaluation and comparison of the technical proposals should concern the effectiveness of the proposal submitted by the bidder in meeting the needs of the contracting authority, including the following:

(a) Technical soundness;

(b) Operational feasibility;

(c) Quality of services and measures to ensure their continuity;

(d) Social and economic-development potential offered by the proposals.

Recommendation 23. The criteria for the evaluation and comparison of the financial and commercial proposals may include, as appropriate:

(a) The present value of the proposed tolls, fees, and other charges over the concession period;

(b) The present value of the proposed direct payments by the contracting authority, if any;

(c) The costs for design and construction activities, annual operation and maintenance costs, present value of capital costs and operating and maintenance costs;

(d) The extent of financial support, if any, expected from the Government;

(e) Soundness of the proposed financial arrangements;

(f) The extent of acceptance of the proposed contractual terms.

Submission, opening, comparison and evaluation of proposals

Recommendation 24. The contracting authority may establish thresholds with respect to quality, technical and commercial aspects to be reflected in the proposals in accordance with the criteria as set out in the request for proposals. Proposals which fail to achieve the thresholds should be regarded as non-responsive.

Recommendation 25. Whether or not it has used preselection proceedings the contracting authority may retain the right to require the bidders to demonstrate again their qualifications in accordance with criteria and procedures set forth in the request for proposals or the preselection documents, as appropriate. Where preselection proceedings have been used, the criteria shall be the same as those used in the preselection proceedings.

Final negotiations

Recommendation 26. The contracting authority should rank all responsive proposals on the basis of the evaluation criteria set forth in the request for proposals and invite for final negotiation of the project agreement the bidder that has attained the best rating. Final negotiations may not concern those terms of the contract that were stated as non-negotiable in the final request for proposals.

Recommendation 27. If it becomes apparent to the awarding authority that the negotiations with the bidder invited will not result in a project agreement, the awarding authority should inform that bidder that it is terminating the negotiations and then invite for negotiations the other bidders on the basis of their ranking until it arrives at a project agreement or rejects all remaining proposals.

Direct negotiations (see chap. III, Selection of the concessionaire", paras. 85-96)

Recommendation 28. The law should set forth the exceptional circumstances under which the contracting authority may be authorized by a higher authority to select the concessionaire through direct negotiations, such as:

(a) When there is an urgent need for ensuring continuity in the provision of the service, and engaging in a competitive selection procedure would therefore be impractical;

(b) In case of projects of short duration and with an anticipated initial investment value not exceeding a specified low amount;

(c) Reasons of national defence or national security;

(d) Cases where there is only one source capable of providing the required service (e.g. because it requires the use of patented technology or unique know-how);

(e) When an invitation to the preselection proceedings or a request for proposals has been issued but no applications or proposals were submitted or all proposals failed to meet the evaluation criteria set forth in the request for proposals, and in the judgement of the contracting authority issuing a new request for proposals would be unlikely to result in a project award;

(f) Other cases where the higher authority authorizes such an exception for compelling reasons of public interest.

Recommendation 29. The law may require that the following procedures be observed in direct negotiations:

(a) The contracting authority should publish a notice of the negotiation proceedings and engage in negotiations with as many companies judged capable of carrying out the project as circumstances permit;

(b) The contracting authority should establish and make known to bidders the qualification criteria and the criteria for evaluating the proposals and determine the relative weight to be accorded to each such criterion and the manner in which they are to be applied in the evaluation of the proposals;

(c) The contracting authority should treat proposals in a manner which avoids the disclosure of their contents to competing bidders;

(d) Any such negotiations between the contracting authority and bidders should be confidential and one party to the negotiations should not reveal to any other person any technical, price or other commercial information relating to the negotiations without the consent of the other party;

(e) Following completion of negotiations, the contracting authority should request all bidders remaining in the proceedings to submit, by a specified date, a best and final offer with respect to all aspects of their proposals;

(f) Proposals should be evaluated and ranked according to the criteria for the evaluation of proposals established by the contracting authority.

Unsolicited proposals (see chap. III, Selection of the concessionaire", paras. 97-117)

Recommendation 30. By way of exception to the selection procedures described in legislative recommendations 12 to 25, the contracting authority may be authorized to handle unsolicited proposals pursuant to specific procedures established by the law for handling unsolicited proposals, provided that such proposals should not relate to a project for which selection procedures have been initiated or announced by the contracting authority.

Procedures for determining the admissibility of unsolicited proposals

Recommendation 31. Following receipt and preliminary examination of an unsolicited proposal, the contracting authority should inform the proponent, within a reasonably short period, whether or not there is a potential public interest in the project. If the project is found to be in the public interest, the contracting authority should invite the proponent to submit a formal proposal in sufficient detail to allow the contracting authority to properly evaluate the concept or technology and determine whether the proposal meets the conditions set forth in the law and is likely to be successfully implemented at the scale of the proposed project.

Recommendation 32. The proponent should retain title to all documents submitted throughout the procedure, and those documents should be returned to it in the event the proposal is rejected.

Procedures for handling unsolicited proposals which do not involve proprietary concepts or technology

Recommendation 33. The contracting authority should initiate competitive selection procedures under recommendations 12 to 25 above if it is found that the envisaged output of the project can be achieved without the use of a process, design, methodology or engineering concept for which the author of the unsolicited proposal possesses exclusive rights or if the proposed concept or technology is not truly unique or new. The author of the unsolicited proposal should be invited to participate in such proceedings and might be given a premium for submitting the proposal.

Procedures for handling unsolicited proposals involving proprietary concepts or technology

Recommendation 34. If it appears that the envisaged output of the project cannot be achieved without using a process, design, methodology or engineering concept for which the author of the unsolicited proposal possesses exclusive rights, the contracting authority should seek to obtain elements of comparison for the unsolicited proposal. For that purpose, the contracting authority should publish a description of the essential output elements of the proposal with an invitation for other interested parties to submit alternative or comparable proposals within a certain reasonable period.

Recommendation 35. The contracting authority may engage in negotiations with the author of the unsolicited proposal if no alternative proposals are received, subject to approval by a higher authority. If alternative proposals are submitted, the contracting authority should invite all the proponents to negotiations in accordance with the provisions of legislative recommendation 27 (b) to (f).

Review procedures (see chap. III, Selection of the concessionaire", paras. 118-122)

Recommendation 36. Bidders who claim to have suffered, or who may suffer, loss or injury due to a breach of a duty imposed on the contracting authority by the law may seek review of the contracting authority's acts in accordance with the laws of the host country.

Notice of project award (see chap. III, Selection of the concessionaire", para. 123)

Recommendation 37. The contracting authority should cause a notice of the award of the project to be published. The notice should identify the concessionaire and include a summary of the essential terms of the project agreement.

Record of selection and award proceedings (see chap. III, Selection of the concessionaire", paras. 124-130)

Recommendation 38. The contracting authority should keep an appropriate record of key information pertaining to the selection and award proceedings. The law should set forth the public access requirements.

IV. CONSTRUCTION AND OPERATION OF INFRASTRUCTURE

General provisions on the project agreement (see chap. IV, "Construction and operation of infrastructure", paras. 1-11)

Recommendation 39. The law might identify the core terms to be provided in the project agreement which may include those terms referred to in recommendations 39 to 65 below.

Recommendation 40. Unless otherwise provided, the project agreement is governed by the law of the host country.

Organization of the concessionaire (see chap. IV, "Construction and operation of infrastructure", paras. 12-18)

Recommendation 41. The contracting authority should have the option to require that the selected bidders establish an independent legal entity with a seat in the country.

Recommendation 42. The project agreement should specify the minimum capital of the project company and the procedures for obtaining the approval of the contracting authority to its statutes and by-laws of the project company and fundamental changes therein.

The project site and easements (see chap. IV, "Construction and operation of infrastructure", paras. 19-32)

Recommendation 43. The project agreement should specify, as appropriate, which assets will be public property and which assets will be the private property of the concessionaire. The project agreement should identify which assets the concessionaire is required to transfer to the contracting authority or to a new concessionaire upon expiry or termination of the project agreement; which assets the contracting authority, at its option, may purchase from the concessionaire; and which assets the concessionaire may freely remove or dispose of upon expiry or termination of the project agreement.

Recommendation 44. The contracting authority should assist the concessionaire in the acquisition of easements needed for the operation, construction and maintenance of the facility. The law might empower the concessionaire to enter upon, transit through, do work or fix installations upon, property of third parties, as required for the construction and operation of the facility.

Financial arrangements (see chap. IV, "Construction and operation of infrastructure", paras. 33-51)

Recommendation 45. The law should enable the concessionaire to collect tariffs or user fees for the use of the facility or the services it provides. The project agreement should provide for methods and formulas for the adjustment of those tariffs or user fees.

Recommendation 46. Where the tariffs or fees charged by the concessionaire are subject to external control by a regulatory body, the law should set forth the mechanisms for periodic and extraordinary revisions of the tariff adjustment formulas.

Recommendation 47. The contracting authority should have the power, where appropriate, to agree to make direct payments to the concessionaire as a substitute for, or in addition to, service charges to be paid by the users or to enter into commitments for the purchase of fixed quantities of goods or services.

Security interests (see chap. IV, "Construction and operation of infrastructure", paras. 52-61)

Recommendation 48. The concessionaire should be responsible for raising the funds required to construct and operate the infrastructure facility and, for that purpose, should have the right to secure any financing required for the project with a security interest in any of its property, with a pledge of shares of the project company, with a pledge of the proceeds and receivables arising out of the concession, or with other suitable security, without prejudice to any rule of law that might prohibit the creation of security interests in public property in the possession of the concessionaire.

Assignment of the concession (see chap. IV, "Construction and operation of infrastructure", paras. 62-63)

Recommendation 49. The project agreement should set forth the conditions under which the contracting authority might give its consent to an assignment of the concession, including the acceptance by the new concessionaire of all obligations under the project agreement and evidence of the new concessionaire's technical and financial capability as necessary for providing the service. The concession should not be assigned to third parties without the consent of the contracting authority .

Transfer of controlling interest in the project company (see chap. IV, "Construction and operation of infrastructure", paras. 64-68)

Recommendation 50. The transfer of a controlling interest in the capital of a concessionaire company may require the consent of the contracting authority.

Construction works (see chap. IV, "Construction and operation of infrastructure", paras. 69-79)

Recommendation 51. The project agreement should set forth the procedures for the review and approval of construction plans and specifications by the contracting authority, the contracting authority's right to monitor the

construction of, or improvements to, the infrastructure facility, the conditions under which the contracting authority may order variations in respect of construction specifications and the procedures for testing and final inspection, approval and acceptance of the facility, its equipment and appurtenances.

Infrastructure operation (see chap. IV, "Construction and operation of infrastructure", paras. 80-97)

Recommendation 52. The project agreement should set forth, as appropriate, the extent of the concessionaire's obligations to ensure:

(a) The adaptation of the service so as to meet the actual demand for the service;

(b) The continuity of the service;

(c) The availability of the service under essentially the same conditions to all users;

(d) The non-discriminatory access, as appropriate, of other service providers to any public infrastructure network operated by the concessionaire.

Recommendation 53. The project agreement should set forth:

(a) The extent of the concessionaire's obligation to provide the contracting authority or a regulatory body, as appropriate, with reports and other information on its operations;

(b) The procedures for monitoring the concessionaire's performance and for taking such reasonable actions as the contracting authority or a regulatory body may find appropriate, to ensure that the infrastructure facility is properly operated and the services are provided in accordance with the applicable legal and contractual requirements.

Recommendation 54. The concessionaire should have the right to issue and enforce rules governing the use of the facility, subject to the approval of the contracting authority or a regulatory body.

General contractual arrangements (see chap. IV, "Construction and operation of infrastructure", paras. 98-150)

Recommendation 55. The contracting authority may reserve the right to review and approve major contracts to be entered into by the concessionaire, in particular contracts with the concessionaire's own shareholders or related persons. The contracting authority's approval should not normally be withheld except where the contracts contain provisions inconsistent with the project agreement or manifestly contrary to the public interest or to mandatory rules of a public law nature.

Recommendation 56. The concessionaire and its lenders, insurers and other contracting partners should be free to choose the law applicable to govern their contractual relations, except where such a choice would violate the host country's public policy.

Recommendation 57. The project agreement should set forth:

(a) The forms, duration and amounts of the guarantees of performance that the concessionaire may be required to provide in connection with the construction and the operation of the facility;

(b) The insurance policies that the concessionaire may be required to maintain;

(c) The compensation to which the concessionaire may be entitled following the occurrence of legislative changes or other changes in the economic or financial conditions that render the performance of the obligation substantially more onerous than originally foreseen. The project agreement should further provide mechanisms for revising the terms of the project agreement following the occurrence of any such changes;

(d) The extent to which either party may be exempt from liability for failure or delay in complying with any obligation under the project agreement due to circumstances beyond their reasonable control;

(e) Remedies available to the contracting authority and the concessionaire in the event of default by the other party.

Recommendation 58. The project agreement should set forth the circumstances under which the contracting authority may temporarily take over the operation of the facility for the purpose of ensuring the effective and uninterrupted delivery of the service in the event of serious failure by the concessionaire to perform its obligations.

Recommendation 59. The contracting authority should be authorized to enter into agreements with the lenders providing for the appointment, with the consent of the contracting authority, of a new concessionaire to perform under the existing project agreement if the concessionaire seriously fails to deliver the service required or if other specified events occur that could justify the termination of the project agreement.

V. DURATION, EXTENSION AND TERMINATION OF THE PROJECT AGREEMENT

Duration and extension of the project agreement (see chap. V, "Duration, extension and termination of the project agreement", paras. ___)

Recommendation 60. The duration of the concession should be specified in the project agreement.

Recommendation 61. The term of the concession should not be extended, except for those circumstances specified in the law, such as:

(a) Completion delay or interruption of operation due to the occurrence of circumstances beyond either party's reasonable control;

(b) Project suspension brought about by acts of the contracting authority or other public authorities;

(c) To allow the concessionaire to recover additional costs arising from requirements of the contracting authority not originally foreseen in the project agreement which the concessionaire would not be able to recover during the normal term of the project agreement.

Termination of the project agreement (see chap. V, "Duration, extension and termination of the project agreement", paras. ___)

Termination by the contracting authority

Recommendation 62. The contracting authority should have the right to terminate the project agreement:

(a) In the event that it can no longer be reasonably expected that the concessionaire will be able or willing to perform its obligations, due to insolvency, serious default or otherwise;

(b) For reasons of public interest, subject to payment of compensation to the concessionaire.

Termination by the concessionaire

Recommendation 63. The concessionaire should have the right to terminate the project agreement under exceptional circumstances specified in the law, such as:

(a) In the event of serious default by the contracting authority or other public authority as regards the fulfilment of their obligations under the project agreement;

(b) In the event that the concessionaire's performance is rendered substantially more onerous as a result of variation orders or other acts of the contracting authority, unforeseen changes in conditions or acts of other public authorities and that the parties have failed to agree on an appropriate revision of the project agreement.

Termination by either party

Recommendation 64. Either party should have the right to terminate the project agreement in the event that the performance of its obligations is rendered impossible by the occurrence of circumstances beyond either party's reasonable control. The parties should further have the right to terminate the project agreement by mutual consent.

Consequences of expiry or termination of the project agreement (see chap. V, "Duration, extension and termination of the project agreement", paras. ___)

Transfer of assets to the contracting authority or to a new concessionaire

Recommendation 65. The project agreement should lay down the criteria for establishing, as appropriate, the compensation to which the concessionaire may be entitled in respect of assets transferred to the contracting authority or to a new concessionaire or purchased by the contracting authority upon expiry or termination of the project agreement.

Financial arrangements upon termination

Recommendation 66. The project agreement should stipulate how compensation due to either party in the event of termination of the project agreement is to be calculated, providing, where appropriate, for compensation for the fair value of works performed under the project agreement, and for losses, including lost profits.

Wind-up and transfer measures

Recommendation 67. The project agreement should set out, as appropriate, the rights and obligations of the parties with respect to:

(a) The transfer of technology required for the operation of the facility;

(b) The training of the contracting authority's personnel or of a successor concessionaire in the operation and maintenance of the facility;

(c) The provision, by the concessionaire, of operation and maintenance services and the supply of spare parts, if required, for a reasonable period after the transfer of the facility to the contracting authority or to a successor concessionaire.

VI. SETTLEMENT OF DISPUTES

Disputes between the contracting authority and the concessionaire (see chap. VI, "Settlement of disputes", paras. ___)

Recommendation 68. The contracting authority should be free to agree to dispute settlement mechanisms regarded by the parties as suited to the needs of the project, including arbitration.

[*Recommendation 68 bis.* The law should indicate whether, and, if so, to what extent the contracting authority may raise a plea of sovereign immunity, both as a bar to the commencement of arbitral or judicial proceedings as well as a defense against enforcement of the award or judgement.]

Disputes between the concessionaire and its lenders, contractors and suppliers (see chap. VI, "Settlement of disputes", paras. ___)

Recommendation 69. The concessionaire should be free to choose the appropriate mechanisms for settling commercial disputes among the project sponsors, or disputes between the concessionaire and its lenders, contractors, suppliers and other business partners.

Disputes between the concessionaire and its customers (see chap. VI, "Settlement of disputes", paras. ___)

Recommendation 70. The concessionaire may be required to make available simplified and efficient mechanisms for handling claims submitted by its customers or users of the infrastructure facility.